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## ACQUISITION FUNDING — TERMINOLOGY AND REQUIREMENTS

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### Antideficiency Act (ADA)

- One of the major laws through which Congress exercises constitutional control of the public purse. Some of its prohibitions include: making or incurring overobligation or overexpenditure from an appropriation, apportionment, or formal subdivision thereof (i.e., allotment or suballotment, if issued, under NASA Fund Control Regulations); making or incurring expenditures or obligations in advance of an appropriation unless authorized by law; and accepting voluntary services unless authorized by law. Additional related restrictions include: only using an appropriation for its intended purpose and, for appropriations made for a definite period (e.g., two-year funds), only using the appropriation for expenses and obligations properly incurred during that time (“bona fide needs” rule). ADA constraints apply to all phases of an appropriation's life cycle.  
*(NASA Procedural Requirements (NPR) 9470.1)*

### CITATIONS:

“one of the major laws through which Congress exercises its constitutional control of the public purse.”  
*(Government Accounting Office's (GAO's) "Antideficiency Act Background")*

(1) An officer or employee of the United States Government or of the District of Columbia government may not—  
(A) make or authorize an expenditure or obligation exceeding an amount available in an appropriation or fund for the expenditure or obligation;  
(B) involve either government in a contract or obligation for the payment of money before an appropriation is made unless authorized by law  
*(31 United States Code (U.S.C.) § 1341(a)(1)(A)&(B))*

(a) An officer or employee of the United States Government or of the District of Columbia government may not make or authorize an expenditure or obligation exceeding—  
(1) an apportionment; or

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(2) the amount permitted by regulations prescribed under section 1514 (a) of this title.

(31 U.S.C. § 1517(a))

Administrative division of apportionments

...subject to the approval of the President, the head of each executive agency (except the Commission) shall prescribe by regulation a system of administrative control not inconsistent with accounting procedures prescribed under law. The system shall be designed to—

(1) restrict obligations or expenditures from each appropriation to the amount of apportionments or reappropriations of the appropriation; and

(2) enable the official or the head of the executive agency to fix responsibility for an obligation or expenditure exceeding an apportionment or reappropriation.

(31 U.S.C. § 1514(a))

D.5.1 Funds appropriated to meet NASA's resource requirements shall be apportioned at the Agency level, allotted at the mission level, and suballotted at the theme level in accordance with the AEP, but always within and in accordance with any controls established in the appropriation and apportionment. Funding targets will be allocated below the suballotment level to facilitate program execution and business operations.

(NPR 9470.1, Attachment D, "NASA Fund Control Regulations")

An officer or employee of the United States Government or of the District of Columbia government may not accept voluntary services for either government or employ personal services exceeding that authorized by law except for emergencies involving the safety of human life or the protection of property.

(31 U.S.C. § 1342)

(a) Appropriations shall be applied only to the objects for which the appropriations were made except as otherwise provided by law.

(31 U.S.C. § 1301(a))

(a) The balance of an appropriation or fund limited for obligation to a definite period is available only for payment of expenses properly incurred during the period of availability or to complete contracts properly made within that period of availability and

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obligated consistent with section 1501 of this title.  
(31 U.S.C. § 1502(a))

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**Bona Fide Need**

- An appropriation or fund limited for obligation to a definite period is available only for payment of expenses properly incurred during the period of availability, or to complete contracts properly made and obligated within the period of availability. That is, the obligation must be to satisfy a need of the agency that arose during the period of availability (with certain limited exceptions) and must meet the purpose and availability of funds established in the appropriation.  
(NPR 9470.1)

**CITATIONS:**

(a) The balance of an appropriation or fund limited for obligation to a definite period is available only for payment of expenses properly incurred during the period of availability or to complete contracts properly made within that period of availability and obligated consistent with section 1501 of this title.  
(31 U.S.C. § 1502(a))

Documentary evidence requirement for Government obligations  
(31 U.S.C. § 1501)

Additional discussion  
(*Principles of Federal Appropriations Law (Red Book)*, Chapter 5.B.)

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**Basic Requirements  
for Funding  
Procurement  
Actions and  
Recording the  
Obligation**

- An obligation is any act that legally binds the Government to make an outlay or expenditure of funds immediately or in the future; a “bona fide” need must exist and funds/budget authority must be available, apportioned, and distributed before creating an obligation. The obligation is recorded in the official accounting system.

The obligation must be made within the fiscal year sought to be charged and must meet a bona fide need of that fiscal year. Obligations are recorded when the precise obligation is known, taking into account the bona fide need requirements. If a precise amount is not known at the time a liability is incurred, an initial

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amount must still be recorded; adjustments to obligations are made when more precise information becomes known.

It does not violate the Bona Fide Needs Rule, the Recording Act, or the ADA to use budget authority to fund an acquisition incrementally within a period of availability, as long as the budget authority equals the obligation by the end of the period, and sufficient funds were available to the Agency at the time of award. Such a practice, however, could lead to a violation of the ADA should funds later be insufficient to cover the requirement, since it would be improper to charge future fiscal years for nonseverable services obligated in a prior year.

#### CITATIONS:

...the general rule for obligating fiscal year appropriations by contract is that the contract imposing the obligation must be made within the fiscal year sought to be charged and must meet a *bona fide* need of that fiscal year. *E.g.*, B-272191, Nov. 4, 1997; B-235086, Apr. 24, 1991; 37 Comp. Gen. 155 (1957)...  
(*Red Book, Chapter 7.B.1*)

As noted previously, where the precise amount of the government's liability is defined at the time the government enters into the contract that is the amount to be recorded. For example, in the simple firm fixed-price contract, the contract price is the recordable obligation. The possibility that the contractor may not perform up to the level specified in the contract does not provide a basis for recording less than the full contract price as the obligation. However, for many types of obligations, the precise amount of the government's liability cannot be known at the time the liability is incurred. As summarized in our preliminary discussion of 31 U.S.C. § 1501(a), some initial amount must still be recorded. The agency should then adjust this initial obligation amount up or down periodically as more precise information becomes available.[12]...

[n.12 This discussion addresses the amount to be recorded when the amount of the liability is undefined, and is not to be confused with a discussion of contingent liabilities. For example, for an indefinite-delivery, indefinite-quantity contract, any liability in excess of the government's minimum commitment, as defined in the contract, is a contingent liability— that is, contingent on the

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government placing future orders with the contractor. For that reason, at the time the government enters into the contract, the government has no liability above the minimum specified in the contract, and thus incurs no obligation for future orders. We discuss contingent liabilities in section C of this chapter.]

*(Red Book, Chapter 7.B.1.f.)*

\* \* \* IN ORDER TO OBLIGATE A FISCAL YEAR APPROPRIATION FOR PAYMENTS TO BE MADE IN A SUCCEEDING YEAR, THE CONTRACT IMPOSING THE OBLIGATION MUST HAVE BEEN MADE WITHIN THE FISCAL YEAR SOUGHT TO BE CHARGED AND THE CONTRACT MUST HAVE BEEN MADE TO MEET A BONA FIDE NEED OF THE FISCAL YEAR TO BE CHARGED. 20 COMP. GEN. 437; 27 ID. 764; CF. 23 ID. 370; ID. 490.  
*(37 Comp. Gen. 155/GAO Decision B-130815)*

(a) If the contract is fully funded, funds are obligated to cover the price or target price of a fixed-price contract or the estimated cost and any fee of a cost-reimbursement contract.

(b) If the contract is incrementally funded, funds are obligated to cover the amount allotted and any corresponding increment of fee.  
*(Federal Acquisition Regulations (FAR) 32.703-1)*

...The question as to whether these obligations were "properly chargeable" to the expired fiscal year 1993 O&M appropriation hinges upon whether these obligations meet the time, purpose, and amount requirements imposed on the fiscal year 1993 O&M appropriation. See 73 Comp. Gen. 338 (1994); B-265901, Oct. 17, 1997. The Congress has provided that expired appropriations remain available for, among other things, "recording . . . obligations properly chargeable" to that appropriation. The House Committee on Government Operations explained:

"Obligations are 'properly chargeable' to an expired account when they reflect 'bona fide needs' of the period of availability of the expired account . . . and meet other requirements set forth in statutes and Comptroller General and court decisions for obligations of appropriated funds."

*(GAO Decision B-272191)*

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The Comptroller of the Navy requested a GAO opinion as to the proper manner in which to record certain obligations of the Navy Industrial Fund in connection with a program to build or convert and charter ships. The Navy's principal concern was with the total amount that should be recorded as a firm government obligation. GAO noted that two contracts govern the Navy's obligation under the program. The first, the agreement to charter, is effective upon signing and obligates the Navy to accept delivery of vessels which conform to the specifications of the contract... The second contract, the charter party agreement, is entirely contingent upon the completion of the first contract and the Navy's obligation does not commence until it has accepted delivery of the vessels.  
*(62 Comp. Gen. 143, 146/GAO Decision B-174839)*

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**Commercial Space  
Launch Act  
(CSLA)  
Agreements**

- An agreement awarded to meet the purpose of the CSLA. See NID 9090.1 on Commercial Services Pricing for additional information.
- (b) Purposes.**— The purposes of this chapter are—  
(1) to promote economic growth and entrepreneurial activity through use of the space environment for peaceful purposes;  
(2) to encourage the United States private sector to provide launch vehicles, reentry vehicles, and associated services...  
*(49 U.S.C. § 70101)*
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**Contingent Liability**

- An existing condition, situation, or set of circumstances which poses the possibility of a loss to an agency that will ultimately be resolved when one or more future events occur or fail to occur.

A contingent liability does not create an obligation unless and until the contingency materializes. However, agencies have a legal obligation to take reasonable steps to avoid situations in which contingent liabilities become actual liabilities that result in Antideficiency Act violations. This may include the “administrative reservation” or “commitment” of funds, as well as taking other actions to prevent contingencies from materializing.

**CITATIONS:**

An existing condition, situation, or set of circumstances which poses the possibility of a loss to an agency that will ultimately be resolved when one or more future events occur or fail to occur.  
*(GAO’s “A Glossary of Terms Used in the Federal Budget*

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*Process”)*

While the precise amount of the liability may be undefined initially, an “obligational event,” reflecting a definite liability, may occur even though the amount of the liability at that time is undefined. A “contingent liability” is fundamentally different. In contrast to a definite liability, a contingent liability does not create an obligation unless and until the contingency materializes...

The contingent liability poses somewhat of a fiscal dilemma. On the one hand, it is by definition (and absent special statutory treatment) not sufficiently definite to support the recording of an obligation. Yet on the other hand, sound financial management may dictate that it somehow be recognized. Indeed, if completely disregarded, a contingent liability could mature into an actual liability and result in an Antideficiency Act violation. Agencies have a legal obligation to take reasonable steps to avoid situations in which contingent liabilities become actual liabilities that result in Antideficiency Act violations. This may include the “administrative reservation” or “commitment” of funds, as well as taking other actions to prevent contingencies from materializing.[35]...

In addition to the obligational accounting treatment of contingent liabilities, agencies need to be aware of the financial accounting treatment of contingent liabilities. Contingent liabilities may be sufficiently important to warrant recognition in a footnote to pertinent financial statements. 62 Comp. Gen. 143, 146 (1983); 37 Comp. Gen. at 692...

[n. 35 See 7 GAO-PPM § 3.5.F; B-238201, Apr. 15, 1991 (nondecision letter).]

*(Red Book, Chapter 7.C.)*

...Projected cost overruns between the target and ceiling prices of a fixed- price-incentive contract are not de facto obligations...

Until the contractor has a legal right to be paid for costs incurred, potential cost overruns are contingent liabilities...

... In this case, the Air Force initially obligated an amount equal to the target price of the contract, which is the accepted practice. In terms of appropriation accounting, the difference between the

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target and ceiling prices is a contingent liability that may or may not require future obligations...

... While there is no Antideficiency Act violation in the current facts, the Air Force failed to commit funds for reasonably predictable cost overruns. We pointed out as long ago as 1955 that when an obligation is recorded at the target price, failure to reserve funds up to the ceiling price exposes the contracting agency to the risk of an Antideficiency Act violation.” 34 Comp. Gen. 418 (1955)...  
(GAO Decision B-255831)

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**Continuing  
Resolution**

- An appropriation act that provides budget authority for the continuation of operations when a regular appropriation act has not been enacted. Continuing resolutions typically incorporate by reference the same restrictions and conditions from regular apportionments.

The continuing resolution appropriates an annual amount, and bona fide need and obligation requirements are typically the same as under a regular appropriation. Thus, a contract severable by fiscal year should be funded for services through September 30 of the current fiscal year or through the end of the period of performance, whichever comes first, if the funding is available. However, exceptions may apply; for example, severable service contracts may be funded through the end of the continuing resolution if necessary to comply with the limitations set forth in the legislation and if an availability of funds clause is contained in the contract.

**CITATIONS:**

An appropriation act that provides budget authority for federal agencies, specific activities, or both to continue in operation when Congress and the President have not completed action on the regular appropriation acts by the beginning of the fiscal year. Enacted in the form of a joint resolution, a continuing resolution is passed by both houses of Congress and signed into law by the President. A continuing resolution may be enacted for the full year, up to a specified date, or until regular appropriations are enacted. (GAO’s “A Glossary of Terms Used in the Federal Budget Process”)

...continuing resolutions typically incorporate by reference restrictions and conditions from regular appropriations acts...

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The “traditional” form, used consistently except for a few years in the 1980s, employs essentially standard language and is clearly a temporary measure. An example of this form is Public Law 108-309...

“SEC. 102. Appropriations made by section 101 shall be available to the extent and in the manner which would be provided by the pertinent appropriations Act.”

*(Red Book, Chapter 10.A.1.)*

The current rate, as that term is used in continuing resolutions, is equivalent to the total amount of money which was available for obligation for an activity during the fiscal year immediately prior to the one for which the continuing resolution is enacted.

*(Red Book, Chapter 10.B.1.)*

When a resolution appropriates funds to continue an activity at a rate for operations “not in excess of the current rate,” the amount of funds appropriated by the resolution is equal to the current rate less any unobligated balance carried over into the present year

*(Red Book, Chapter 10.B.2.)*

Continuing resolutions are often enacted to cover a limited period of time, such as a month or a calendar quarter. The time limit stated in the resolution is the maximum period of time during which funds appropriated by the resolution are available for obligation.

However, this limited period of availability does not affect the amount of money appropriated by the resolution. The rate for operations specified in the resolution, whether in terms of an appropriation act which has not yet become law, a budget estimate, or the current rate, is an annual amount. The continuing resolution, in general, regardless of its period of duration, appropriates this full annual amount...

*(Red Book, Chapter 10.B.3.)*

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**Contract**

- “Contract” means a mutually binding legal relationship obligating the seller to furnish the supplies or services (including construction) and the buyer to pay for them. It includes all types of commitments that obligate the Government to an expenditure of appropriated funds and that, except as otherwise authorized, are in writing. In addition to bilateral instruments, contracts include (but are not limited to) awards and notices of awards; job orders or task

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letters issued under basic ordering agreements; letter contracts; orders, such as purchase orders, under which the contract becomes effective by written acceptance or performance; and bilateral contract modifications. Contracts do not include grants and cooperative agreements...

*(FAR 2.101)*

While the term “contract” is often used informally to refer to all form of binding agreements, the better practice is to reserve the term for procurement contracts covered under the FAR. This does not include agreements under “other transaction authority,” such as Space Act Agreements or most barter or reimbursable agreements under special authorities like the Commercial Space Launch Act.

#### CITATIONS:

*An other transaction (OT) is a special vehicle used by federal agencies for obtaining or advancing research and development (R&D) or prototypes. An OT is not a contract, grant, or cooperative agreement, and there is no statutory or regulatory definition of “other transaction.”*

*(Congressional Research Service (CRS) Report for Congress: Other Transaction (OT) Authority)*

In April 2000, we reported on the Department of Defense’s (DOD) use of Section 845 agreements, also referred to as “other transactions” for prototype projects. These are transactions other than contracts, grants, or cooperative agreements that generally are not subject to federal laws and regulations applicable to procurement contracts.

*(GAO-03-150)*

**(a)** Except as provided in this section, a payment under a contract to provide a service or deliver an article for the United States Government may not be more than the value of the service already provided or the article already delivered.

**(b)** An advance of public money may be made only if it is authorized by...

*(31 U.S.C. § 3324)*

An executive agency shall use a procurement contract as the legal instrument reflecting a relationship between the United States

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Government and a State, a local government, or other recipient when—

(1) the principal purpose of the instrument is to acquire (by purchase, lease, or barter) property or services for the direct benefit or use of the United States Government; or

(2) the agency decides in a specific instance that the use of a procurement contract is appropriate.

*(31 U.S.C. § 6303)*

§ 11. No contracts or purchases unless authorized or under adequate appropriation; report to the Congress

(a) No contract or purchase on behalf of the United States shall be made, unless the same is authorized by law or is under an appropriation adequate to its fulfillment, except in the Department of Defense and in the Department of Homeland Security with respect to the Coast Guard when it is not operating as a service in the Navy, for clothing, subsistence, forage, fuel, quarters, transportation, or medical and hospital supplies, which, however, shall not exceed the necessities of the current year.

*(41 U.S.C. § 6301 [previously in 41 U.S.C. § 11])*

See “Grant and Cooperative Agreement” and “Space Act Agreement” for descriptions of those documents and their appropriate use.

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**Contract  
Modifications**

— “Contract modification” means any written change in the terms of a contract.

*(FAR 2.101)*

Contracts should be funded on a set cycle to minimize the number of funding actions, preferably no more frequently than quarterly. In addition, except to fully fund a contract, incremental funding modifications and modifications to deobligate funds shall not be issued for amounts totaling less than \$25,000.

The Procurement Officer, with the Chief Financial Officer’s concurrence, may waive the \$25,000 minimum for contract modifications.

**CITATIONS:**

If the modification exceeds the general scope of the original contract, for example, by increasing the quantity of items to be

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delivered, the modification amounts to a new obligation and is chargeable to funds current at the time the modification is made. 37 Comp. Gen. 861 (1958); B-207433, Sept. 16, 1983...

In the case of a contract for severable services, a modification providing for increased services must be charged to the fiscal year or years in which the services are rendered...

*(Red Book, Chapter 5.B.7.)*

NASA policy.

(d) Except for a modification issued to fully fund a contract, incremental funding modifications shall not be issued for amounts totaling less than \$25,000.

(e) Except for a modification issued to close out a contract, modifications deobligating funds shall not be issued for amounts totaling less than \$25,000.

(f) The procurement officer, with the concurrence of the installation Comptroller, may waive any of the conditions set forth in paragraphs 1832.702-70(a) through (e). The procurement officer shall maintain a record of all such approvals during the fiscal year.

*(NASA FAR Supplement (NFS) 1832.702-70)*

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**Contract Period of  
Performance or  
Term**

— For all severable services contracts, the basic period of performance shall not extend beyond the date of the availability of funds initially obligated to the contract at the time of the award. The Bona Fide Needs Rule, codified at 31 U.S.C. § 1502, also provides that an appropriations or fund with a definite period is available for obligation on contracts properly made within that period of availability for services to be provided during that period of availability. The period of performance of any options on severable services contracts shall not extend beyond the period of availability of the funds corresponding to the exercise of the option.

*(NASA Procurement Information Circular 11-05)*

**CITATIONS:**

(a) The balance of an appropriation or fund limited for obligation to a definite period is available only for payment of expenses properly incurred during the period of availability or to complete contracts properly made within that period of availability and

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obligated consistent with section 1501 of this title. However, the appropriation or fund is not available for expenditure for a period beyond the period otherwise authorized by law.  
(31 U.S.C. § 1502)

**Contracts crossing fiscal years.**

- (a) A contract that is funded by annual appropriations may not cross fiscal years, except in accordance with statutory authorization (*e.g.*, 41 U.S.C. 11a, 31 U.S.C. 1308, 42 U.S.C. 2459a, 42 U.S.C. 3515, and paragraph (b) of this subsection) [*Note: Content in 41 U.S.C. § 11a is now covered in*
- (b) *41 U.S.C. § 6302; 42 U.S.C. 2459a has been eliminated*], or when the contract calls for an end product that cannot feasibly be subdivided for separate performance in each fiscal year (*e.g.*, contracts for expert or consultant services).

(b) The head of an executive agency, except NASA, may enter into a contract, exercise an option, or place an order under a contract for severable services for a period that begins in one fiscal year and ends in the next fiscal year if the period of the contract awarded, option exercised, or order placed does not exceed one year (10 U.S.C. 2410a and 41 U.S.C. 2531) [*Note: Content in 41 U.S.C. § 2531 is now covered in 41 U.S.C. § 3902*]. Funds made available for a fiscal year may be obligated for the total amount of an action entered into under this authority.  
(FAR 32.703-3)

**Funding and term of service contracts.**

(a) When contracts for services are funded by annual appropriations, the term of contracts so funded shall not extend beyond the end of the fiscal year of the appropriation except when authorized by law (see paragraph (b) of this section for certain service contracts, 32.703-2 for contracts conditioned upon availability of funds, and 32.703-3 for contracts crossing fiscal years).

(b) The head of an executive agency, except NASA, may enter into a contract, exercise an option, or place an order under a contract for severable services for a period that begins in one fiscal year and ends in the next fiscal year if the period of the contract awarded, option exercised, or order placed does not exceed one year (10 U.S.C. 2410a and 41 U.S.C. 2531) [*Note: Content in 41 U.S.C. § 2531 is now covered in 41 U.S.C. § 3902*]. Funds

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made available for a fiscal year may be obligated for the total amount of an action entered into under this authority.

(c) Agencies with statutory multiyear authority shall consider the use of this authority to encourage and promote economical business operations when acquiring services.

(FAR 37.106)

Apart from the extended period of availability, multiple year appropriations are subject to the same principles applicable to annual appropriations and do not present any special problems.

(Red Book, Chapter 5.A.2.b.)

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**Contractual  
Services and  
Supplies**

- The obligation for contractual services and supplies is incurred at the time that there is a binding agreement, usually when the contract is signed. This will generally be the maximum liability to the Government within the limitations set forth in the contract terms and considering bona fide need requirements.

**CITATIONS:**

**20.5 When should I record obligations and in what amounts?**

(c) *Contractual services and supplies.*

Services and supplies that are purchased by contract are recorded as obligations at the time there is a binding agreement, which is usually when the contract is signed. As a general rule, the amount of the obligation is the maximum liability to the Federal Government. The maximum liability to the Government is normally limited by the terms of the contract (e.g., cancellation clauses).

The following provides the nuances of contracts with certain characteristics.

Contracts with...	Amount obligated is...	At the time ...
A maximum price	The maximum price	The contract is signed.

	Amount of downward adjustments (i.e. deobligation), if any	There is documentary evidence that the price is reduced.
Letters of intent and letter contracts	Normally, no amount is obligated	The letter is signed.
However, if the letters constitute binding agreements under which the contractor is authorized to proceed	The maximum amount indicated in the letter that the contractor is authorized to incur to cover expenses prior to the execution of a definitive contract	
Contracts for variable quantities	Normally, no amount is obligated	The contract is signed.
The contracts are usually followed by "purchase orders" that do obligate the Government	The amount of actual orders	The order is issued.
Orders where a law "requires" that you to place orders with another Federal Government account	The amount of the order	The order is issued.
Voluntary orders with other Federal Government accounts:	The amount of the order	The order is issued.

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If the order is for common-use standard stock item the supplier has on hand or on order at published prices

That you issue the order to the supplier.

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If the order is for stock items other than the above

You receive a formal notification that the items are on hand or on order

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If the order involves execution of a specific contract

The supplying agency notifies you that it has entered into the contract.

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*(Office of Management and Budget (OMB) Circular No. A-11, Section 20.5)*

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**Cost Reimbursement**

- A cost-reimbursement contract provides for payment of allowable incurred costs, to the extent prescribed in the contract, and establishes an estimate of total cost for the purpose of obligating funds and establishing a ceiling that the contractor may not exceed without the approval of the contracting officer. The following are types of cost-reimbursement contracts:
- Cost contract – the contractor receives no fee.
  - Cost-sharing contract – the contractor receives no fee and is reimbursed only for an agreed-upon portion of its allowable costs.
  - Cost-plus-incentive fee contract – provides for an initially negotiated fee to be adjusted later by a formula based on the relationship of total allowable costs to total target costs.
  - Cost-plus-award-fee contract – provides for a fee consisting of a base amount (which may be zero) fixed at inception of the contract and an award amount sufficient to provide motivation for excellence in contract performance.
  - Cost-plus-fixed-fee contract – provides for payment to the



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contractor of a negotiated fee that is fixed at the inception of the contract.

The funding requirements for cost-reimbursement contracts vary depending on whether they are severable or nonseverable. Nonseverable tasks must be fully funded by an appropriation available for obligation (current) at the time of award. Severable services must be funded by an appropriation available at the time the services are provided.

Cost-reimbursement contracts may be incrementally funded only if otherwise legally authorized and if all of the following conditions are met:

- Total contract value, including options, is \$500,000 or more for R&D contracts under which no supplies are deliverable; or \$1,000,000 or more for all other contracts.
- Period of performance is greater than one year.
- Funds are not available to fully fund at the time of award.
- Initial funding is greater than \$100,000.

The Procurement Officer, with the Chief Financial Officer's concurrence, may waive the conditions for incremental funding set forth in NFS 1832.702-70 and listed in the preceding paragraph.

#### CITATIONS:

- (a) If the contract is fully funded, funds are obligated to cover the price or target price of a fixed-price contract or the estimated cost and any fee of a cost-reimbursement contract.
- (b) If the contract is incrementally funded, funds are obligated to cover the amount allotted and any corresponding increment of fee. (*FAR 32.703-1*)

...for many types of obligations, the precise amount of the government's liability cannot be known at the time the liability is incurred. As summarized in our preliminary discussion of 31 U.S.C. § 1501(a), some initial amount must still be recorded. The agency should then adjust this initial obligation amount up or down periodically as more precise information becomes available.[12]

GAO decisions, as well as GAO's *Policy and Procedures Manual*

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*for Guidance of Federal Agencies*,<sup>13</sup> indicate that, in general, the agency should use its best estimate to record the initial amount where the amount of the government's final liability is undefined. *E.g.*, 56 Comp. Gen. 414, 418 (1977); 50 Comp. Gen. 589 (1971). Section 3.5.D of the *Manual* further provides that, where an estimate is used, the basis for the estimate and the computation must be documented.

[n. 12 This discussion addresses the amount to be recorded when the amount of the liability is undefined, and is not to be confused with a discussion of contingent liabilities...]

*(Red Book, Chapter 7.B.1.f.)*

Under a cost-reimbursement contract, an agency is required to obligate the estimated costs (or ceiling) established in the base year contract for the required services or products at the time of award. When modifications are approved increasing the original funding ceiling in the contract award, the increased costs are charged to the appropriation current at the time of the modification. It is true that modifications of fixed-priced contracts can be charged against the funding available at the time of the original contract award, depending upon the type of contract modification. However, agencies must obligate the ceiling amount under a cost-reimbursement contract based upon a reasonable estimate of costs for providing the service or product. Agencies cannot simply limit the amount of a recorded obligation by stating that the contract is limited to an amount of funding available for the contract or stating that the contract will be incrementally funded if those amounts are different than the estimated ceiling costs.[15]

[n. 15 *See* B-317139, June 1, 2009. In some circumstances, services contracted under cost-reimbursement contracts and other types of contracts may be charged to funding available during subsequent fiscal years. This may depend upon whether the services are severable or nonseverable. *See id.*]

...cost-reimbursement contracts are suitable only when the cost of the work to be done cannot be estimated with sufficient accuracy to use any type of fixed-price contract...

*(GAO-09-921)*

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A nonseverable services contract that is not separated for performance by fiscal year may not be funded on an incremental basis without statutory authority. Failure to obligate the estimated cost (or ceiling) of a nonseverable cost-reimbursement contract at the time of award violated the bona fide needs rule.

Contract modifications to a cost-reimbursement contract increasing original ceiling are chargeable to appropriations available when the modifications were approved by the contracting officer. The actual date the agency records the obligation in its books is irrelevant to the determination of when the obligation arises and what fiscal year appropriation to charge.

A provision in an annual appropriations act designating that a portion of a lump-sum amount “shall be available for” a specific project does not preclude the use of other available appropriations for the project.

*(GAO Decision B-317139)*

DISCRETIONARY COST INCREASES IN COST REIMBURSEMENT CONTRACTS WHICH EXCEED CONTRACTUALLY STIPULATED CEILINGS SET FORTH IN LIMITATION OF COST CLAUSES AND WHICH ARE NOT ENFORCEABLE BY CONTRACTOR ARE PROPERLY CHARGEABLE TO FUNDS AVAILABLE WHEN THE DISCRETIONARY INCREASE IS GRANTED BY THE CONTRACTING OFFICER. 59 COMP.GEN. 518 AND OTHER PRIOR INCONSISTENT DECISIONS ARE MODIFIED ACCORDINGLY...

ON THE QUESTION OF CHANGES WHICH INCREASE THE COST OF THE CONTRACT BUT DO NOT EXCEED THE CONTRACTUALLY SET CEILING, WE CONTINUE TO ADHERE TO THE VIEW THAT SUCH INCREASES SHOULD BE CHARGED TO THE APPROPRIATION AVAILABLE WHEN THE CONTRACT WAS ENTERED. THIS POSITION IS BASED ON THE FACT THAT AN AGENCY MUST RESERVE FUNDS IN THE AMOUNT OF THE CONTRACT'S CEILING AT ITS INCEPTION IN ORDER TO COMPLY WITH THE ANTIDEFICIENCY ACT (31 U.S.C. 665 (1976)) PROHIBITION AGAINST INCURRING OBLIGATIONS IN EXCESS OF

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AVAILABLE APPROPRIATIONS SINCE THE AGENCY IS CONTRACTUALLY BOUND AT THE OUTSET TO FUND ANY COST INCREASES NOT RELATED TO INCREASED WORK TO THE CONTRACT'S CEILING. SINCE THE CEILING AMOUNT MUST BE COMMITTED AT THE CONTRACT'S INCEPTION, ANY UNDER-CEILING COST INCREASES IN LATER YEARS WHICH ARE WITHIN THE CONTRACT'S SCOPE-- WHETHER BECAUSE OF CHANGED WORK OR NOT-- THEREFORE SHOULD BE CONSIDERED AS COVERED BY THE ORIGINAL CONTRACTUAL OBLIGATION...

UPON RECONSIDERATION, WE THEREFORE CONCLUDE THAT COST INCREASES IN COST REIMBURSEMENT CONTRACTS WHICH EXCEED CONTRACTUALLY STIPULATED CEILINGS AND WHICH ARE NOT BASED ON AN ANTECEDENT LIABILITY, ENFORCEABLE BY THE CONTRACTOR, MAY PROPERLY BE CHARGED TO FUNDS AVAILABLE WHEN THE DISCRETIONARY INCREASE IS GRANTED BY THE CONTRACTING OFFICER. ACCORDINGLY, OUR 1980 DECISION, 59 COMP.GEN. 518, IS MODIFIED TO CONFORM TO THIS DECISION, AS ARE OTHER PRIOR DECISIONS INCONSISTENT WITH THIS ONE.

...IN OUR 1980 DECISION, WE CONCLUDED THAT THE COST OF THE 1979 MODIFICATION TO REFLECT AN INCREASE IN ALLOWABLE OVERHEAD RATES WAS TO BE PAID FROM THE ORIGINAL APPROPRIATION OBLIGATED FOR THE CONTRACT, EVEN THOUGH THE MODIFICATION RESULTED IN AN INCREASE IN THE CONTRACT'S COST CEILING. THE BASIS FOR OUR CONCLUSION WAS THAT THE INCREASED OVERHEAD RATES WERE BASED ON AN ANTECEDENT CONTRACTUAL LIABILITY WITHIN THE SCOPE OF THE ORIGINAL CONTRACT...

IN ALL THREE SITUATIONS, EPA WOULD USE CURRENTLY AVAILABLE FUNDS TO PAY INCREASES BEYOND THE ORIGINAL COST CEILING SET OUT IN THE CONTRACT ON THE THEORY THAT THERE IS NO ANTECEDENT LIABILITY, ENFORCEABLE BY THE CONTRACTOR, TO GRANT SUCH INCREASES, AND

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HENCE NO "OBLIGATION" OF ORIGINALLY AVAILABLE FUNDS...

*(61 Comp. Gen. 609/GAO Decision B-195732, which modified 59 Comp. Gen. 518)*

Thus, fairly read, B-235678 stands for the proposition that a CPFF term contract is presumptively a severable service contract, unless the actual nature of the work warrants a different conclusion (i.e., clearly calls for an end product).  
*(GAO Decision B-277165)*

Cost-reimbursement types of contracts provide for payment of allowable incurred costs, to the extent prescribed in the contract. These contracts establish an estimate of total cost for the purpose of obligating funds and establishing a ceiling that the contractor may not exceed (except at its own risk) without the approval of the contracting officer.

Cost-reimbursement contracts are suitable for use only when uncertainties involved in contract performance do not permit costs to be estimated with sufficient accuracy to use any type of fixed-price contract.

*(FAR 16.301-1 and 16.301-2)*

(a) *Description.* A cost contract is a cost-reimbursement contract in which the contractor receives no fee.  
*(FAR 16.302)*

(a) *Description.* A cost-sharing contract is a cost-reimbursement contract in which the contractor receives no fee and is reimbursed only for an agreed-upon portion of its allowable costs.  
*(FAR 16.303)*

A cost-plus-incentive-fee contract is a cost-reimbursement contract that provides for an initially negotiated fee to be adjusted later by a formula based on the relationship of total allowable costs to total target costs. Cost-plus-incentive-fee contracts are covered in Subpart 16.4, Incentive Contracts. See 16.405-1 for a more complete description and discussion of application of these contracts. See 16.301-3 for limitations.  
*(FAR 16.304)*

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A cost-plus-award-fee contract is a cost-reimbursement contract that provides for a fee consisting of (a) a base amount (which may be zero) fixed at inception of the contract and (b) an award amount, based upon a judgmental evaluation by the Government, sufficient to provide motivation for excellence in contract performance. Cost-plus-award-fee contracts are covered in Subpart 16.4, Incentive Contracts. See 16.401(e) for a more complete description and discussion of the application of these contracts. See 16.301-3 and 16.401(e)(5) for limitations.  
(FAR 16.305)

(a) *Description.* A cost-plus-fixed-fee contract is a cost-reimbursement contract that provides for payment to the contractor of a negotiated fee that is fixed at the inception of the contract. The fixed fee does not vary with actual cost, but may be adjusted as a result of changes in the work to be performed under the contract. This contract type permits contracting for efforts that might otherwise present too great a risk to contractors, but it provides the contractor only a minimum incentive to control costs.  
(FAR 16.306)

NASA policy.

(a) Cost-reimbursement contracts may be incrementally funded only if all the following conditions are met:

(1) The total value of the contract (including options as defined in FAR Subpart 17.2) is--

(i) \$500,000 or more for R&D contracts under which no supplies are deliverable; or

(ii) \$1,000,000 or more for all other contracts.

(2) The period of performance exceeds one year.

(3) The funds are not available to fund the total contract value fully at award.

(4) Initial funding of the contract is \$100,000 or more...

(f) The procurement officer, with the concurrence of the installation Chief Financial Officer, may waive any of the conditions set forth in paragraphs 1832.702-70(a) through (f). The Procurement Officer shall maintain a record of all such approvals during the fiscal year.

(NFS 1832.702-70)

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**Economy Act  
Agreement**

- An agreement to obtain goods or services from another agency or major unit of the same agency under the terms of 31 U.S.C. § 1535.

Obligations for services must be funded by an appropriation available for obligation when they are rendered and supplies must be funded by an appropriation available when the order is placed. The amount obligated must be deobligated to the extent that the performing agency/unit has not incurred obligations before the end of the period of availability of the ordering appropriation and set agreement period of performance. Funds may not be obligated by the performing agency after the ordering agency's appropriation expires and set agreement period of performance.

**CITATIONS:**

(a) The head of an agency or major organizational unit within an agency may place an order with a major organizational unit within the same agency or another agency for goods or services if—

(1) amounts are available;

(2) the head of the ordering agency or unit decides the order is in the best interest of the United States Government;

(3) the agency or unit to fill the order is able to provide or get by contract the ordered goods or services; and

(4) the head of the agency decides ordered goods or services cannot be provided by contract as conveniently or cheaply by a commercial enterprise... ///

(d) An order placed or agreement made under this section obligates an appropriation of the ordering agency or unit. The amount obligated is deobligated to the extent that the agency or unit filling the order has not incurred obligations, before the end of the period of availability of the appropriation, in—

(1) providing goods or services; or

(2) making an authorized contract with another person to provide the requested goods or services.

(31 U.S.C. § 1535)

When an ordering agency enters into an Economy Act agreement and incurs an obligation using fiscal year funds, the Economy Act requires the ordering agency to deobligate the appropriation at the end of the fiscal year to the extent that the performing agency has not performed or incurred a valid obligation on behalf of the ordering agency. 31 U.S.C. § 1535(d); 34 Comp. Gen. 418, 419

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(1955).

(GAO's "Frequently Asked Questions Regarding Interagency Transactions")

## 20.5 When should I record obligations and in what amounts?

### (d) *Intragovernmental services and supplies.*

Obligations are incurred for services when they are rendered. For example, obligations for GSA rental payments are incurred in the year in which the premises are occupied, whether or not a bill has been rendered. Obligations are incurred for supplies when the order is placed.

(OMB Circular No. A-11, Section 20.5)

AMOUNTS BASED ON WRITTEN INTRAGOVERNMENT AGREEMENTS AUTHORIZED BY LAW FOR SPECIFIC SUPPLIES AND SERVICES MAY BE RECORDED AS OBLIGATIONS UNDER SECTION 1311 OF THE SUPPLEMENTAL APPROPRIATION ACT, 1955; HOWEVER, OBLIGATIONS AGAINST FISCAL YEAR APPROPRIATIONS BASED ON INTRAGOVERNMENT AGREEMENTS ENTERED INTO PURSUANT TO SECTION 601 OF THE ECONOMY ACT OF 1932 ARE REQUIRED BY SECTION 1210 OF THE GENERAL APPROPRIATION ACT, 1951, TO BE DEOBLIGATED AT THE END OF EACH FISCAL YEAR TO THE EXTENT THAT THE PERFORMING OR PROCURING AGENCY HAS NOT INCURRED VALID OBLIGATIONS UNDER SUCH AGREEMENTS. SECTION 1311 OF THE SUPPLEMENTAL APPROPRIATION ACT, 1955, DOES NOT CHANGE THE CRITERIA SET OUT IN 32 COMP. GEN. 436 FOR THE RECORDING OF OBLIGATIONS FOR STOCK ITEMS.

(34 Comp. Gen. 418/GAO Decision B-121982)

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### **Firm Fixed Price**

- A firm fixed price contract provides for a price that is not subject to any adjustment regardless of the contractor's cost experience in performing the contract. It may be used in conjunction with an award-fee incentive and performance or delivery incentives when the award fee or incentive is based solely on factors other than cost. The contract type remains firm-fixed-price when used with these incentives.



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If the contract is nonseverable, it must be fully funded by an appropriation available for obligation at the time of award. If the contract has more than one nonseverable component, an obligation is recorded as the nonseverable tasks orders are placed. If the contract is for severable services, it must be funded by an appropriation available for obligation at the time the services are provided. The obligation for severable services is for services through September 30 of the current fiscal year or through the end of the period of performance, whichever comes first.

Fixed price contracts other than research and development (R&D) shall not be incrementally funded, with the exception of high technology capital projects, which are highly dependent on R&D and highly uncertain in outcome.

If otherwise legally authorized, fixed price R&D contracts may be incrementally funded if the incremental funding conditions for cost-reimbursement contracts are met and the initial funding increment is at least 50 percent of total fixed price. Fixed price incrementally funded contracts must be fully funded as soon as funding is available.

The Procurement Officer, with the Chief Financial Officer, may waive the conditions for incremental funding set forth in NFS 702-70 and discussed in the preceding paragraph.

See “Fixed Price Incentive” for funding requirements of contracts with incentives.

#### CITATIONS:

As noted previously, where the precise amount of the government’s liability is defined at the time the government enters into the contract that is the amount to be recorded. For example, in the simple firm fixed-price contract, the contract price is the recordable obligation. The possibility that the contractor may not perform up to the level specified in the contract does not provide a basis for recording less than the full contract price as the obligation...

*(Red Book, Chapter 7.B.1.f.)*

(a) If the contract is fully funded, funds are obligated to cover the price or target price of a fixed-price contract or the estimated cost

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and any fee of a cost-reimbursement contract.

(b) If the contract is incrementally funded, funds are obligated to cover the amount allotted and any corresponding increment of fee.  
(FAR 32.703-1)

Fixed-price types of contracts provide for a firm price or, in appropriate cases, an adjustable price. Fixed-price contracts providing for an adjustable price may include a ceiling price, a target price (including target cost), or both. Unless otherwise specified in the contract, the ceiling price or target price is subject to adjustment only by operation of contract clauses providing for equitable adjustment or other revision of the contract price under stated circumstances. The contracting officer shall use firm-fixed-price or fixed-price with economic price adjustment contracts when acquiring commercial items.  
(FAR 16.201)

A firm-fixed-price contract provides for a price that is not subject to any adjustment on the basis of the contractor's cost experience in performing the contract. This contract type places upon the contractor maximum risk and full responsibility for all costs and resulting profit or loss. It provides maximum incentive for the contractor to control costs and perform effectively and imposes a minimum administrative burden upon the contracting parties. The contracting officer may use a firm-fixed-price contract in conjunction with an award-fee incentive (see 16.404) and performance or delivery incentives (see 16.402-2 and 16.402-3) when the award fee or incentive is based solely on factors other than cost. The contract type remains firm-fixed-price when used with these incentives.  
(FAR 16.202-1)

NASA Policy.

(a) Cost-reimbursement contracts may be incrementally funded only if all the following conditions are met:

(1) The total value of the contract (including options as defined in FAR Subpart 17.2) is--

(i) \$500,000 or more for R&D contracts under which no supplies are deliverable; or

(ii) \$1,000,000 or more for all other contracts.

(2) The period of performance exceeds one year.

(3) The funds are not available to fund the total contract value fully at award.

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(4) Initial funding of the contract is \$100,000 or more.

(b) Fixed-price contracts, other than those for research and development, shall not be incrementally funded.

(c)(1) Fixed-price contracts for research and development may be incrementally funded if the conditions of 1832.702-70(a)(1) through (4) are met and the initial funding of the contract is at least 50 percent of the total fixed price.

(2) Incrementally funded fixed-price contracts shall be fully funded as soon as adequate funding becomes available...

(f) The procurement officer, with the concurrence of the installation Chief Financial Officer, may waive any of the conditions set forth in paragraphs 1832.702-70(a) through (f). The Procurement Officer shall maintain a record of all such approvals during the fiscal year.

*(NFS 1832.702-70)*

High technology capital projects are incrementally funded projects for which budget authority is or appears to be provided for only part of the estimated cost of information technology acquisitions or projects that are highly dependent on research and development and highly uncertain in outcome. Space exploration equipment would be an example of such a project. Incremental funding can be justified for high technology capital projects because such projects are often closer in nature to research and development and funding provided on an incremental basis can provide useful knowledge even if no additional funding is provided.

*(GAO-01-432R)*

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**Fixed Price  
Incentive or with  
Economic Price  
Adjustment**

- A fixed price incentive contract is a fixed price contract that provides for adjusting profit and establishing the final contract price based on the contractor's performance. The contract will state a target cost that may be adjusted based upon an incentive provision or formula in the contract. One with an economic price adjustment provides for revision of the stated contract price upon the occurrence of specified contingencies.

If the contract is nonseverable, it must be fully funded by an appropriation current at the time of award. If the contract has more than one nonseverable component, an obligation is recorded as the nonseverable tasks orders are placed. If the contract is for severable services, it must be funded by an appropriation available for obligation at the time the services are provided. The obligation for severable services is for services through September 30 of the

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current fiscal year or through the end of the period of performance, whichever comes first. For a fixed price incentive or with economic price adjustment contract, the target amount is the amount to be obligated, with the obligation adjusted upward as incentive payments become due or price adjustments are made. The difference between the target and ceiling prices is a contingent liability that may or may not require future obligations. The agency should administratively reserve sufficient funds to cover the potential liability and avoid the possibility of a violation of the Antideficiency Act or 41 U.S.C. § 6301.

#### CITATIONS:

Decisions dealing with certain kinds of contract obligations provide more specific rules. Under a fixed-price contract with escalation, price redetermination, or incentive provisions, the amount to be obligated initially is the fixed price stated in the contract or the target price in the case, for example, of a contract with an incentive clause. B-255831, July 7, 1995; 34 Comp. Gen. 418 (1955); B-133170, Jan. 29, 1975; B-206283-O.M., Feb. 17, 1983. Thus, in an incentive contract with a target price of \$85 million and a ceiling price of \$100 million, the proper amount to record initially as an obligation is the target price of \$85 million. 55 Comp. Gen. 812, 824 (1976). *See also McDonnell Douglas Corp. v. United States*, 39 Fed. Cl. 665 (1997). The agency must increase or decrease the amount recorded (*i.e.*, the target price) to reflect price revisions at the time such revisions are made or determined pursuant to the provisions of the contract. 34 Comp. Gen. at 420–21. When obligations are recorded based on a target price, the agency should establish appropriate safeguards to guard against violations of the Antideficiency Act. This usually means the administrative reservation of sufficient funds to cover potential liability.

(*Red Book*, Chapter 7.B.1.f.)

...Termination of a contract prior to incurring obligations in excess of funds available in the appropriation account prevents an Antideficiency Act violation. Projected cost overruns between the target and ceiling prices of a fixed-price-incentive contract are not de facto obligations. Until the contractor has a legal right to be paid for costs incurred, potential cost overruns are contingent liabilities. Air Force regulations permit a procuring entity to limit the initial obligation on a fixed-price-incentive contract to the

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target price... In this case, the Air Force initially obligated an amount equal to the target price of the contract, which is the accepted practice. [12] In terms of appropriation accounting, the difference between the target and ceiling prices is a contingent liability that may or may not require future obligations...

While there is no Antideficiency Act violation in the current facts, the Air Force failed to commit funds for reasonably predictable cost overruns. We pointed out as long ago as 1955 that when an obligation is recorded at the target price, failure to reserve funds up to the ceiling price exposes the contracting agency to the risk of an Antideficiency Act violation. 34 Comp.Gen. 418 (1955)...

[n. 12. See, e.g., Federal Acquisition Regulation, 48 C.F.R. Sec. 32.703-1.]

*(GAO Decision B-255831)*

FIXED-PRICE CONTRACTS WITH ESCALATION, PRICE REDETERMINATION, OR INCENTIVE PROVISIONS SHOULD BE RECORDED AS OBLIGATIONS, PURSUANT TO SECTION 1311 OF THE SUPPLEMENTAL APPROPRIATION ACT, 1955, FOR THE AMOUNT OF THE FIXED PRICE STATED IN THE CONTRACT, OR FOR THE TARGET OR BILLING PRICE IN THE CASE OF THE INCENTIVE CLAUSE CONTRACT, AND THAT AMOUNT INCREASED OR DECREASED TO REFLECT PRICE REVISIONS AT THE TIME SUCH REVISIONS ARE MADE; HOWEVER, IN ORDER TO PREVENT VIOLATION OF THE ANTI- DEFICIENCY ACT SUFFICIENT FUNDS SHOULD BE RESERVED TO COVER THE EXCESS OF THE ESTIMATED INCREASES OVER THE DECREASES.

*(34 Comp. Gen. 418/GAO Decision B-121982)*

...This memorandum is in response to several questions raised by Assistant Regional Manager J.W. Dorris concerning the propriety of certain contract restructuring actions taken by the Army Missile [sic] Command in connection with the Stinger missile [sic] program. The questions and out answers follow.

Question 1: Does the practice, required by Army Regulation (AR) 37-21 Sec. 2-8(b) (May 26, 1977), of recording fixed-price incentive contract obligations at target price, instead of ceiling

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price, violate the Antideficiency Act, 31 U.S.C. Sec. 1341(a) (recently recodified from 31 U.S.C. Sec. 665(a)).

Answer: No, this practice does not violate the Antideficiency Act...

Based on our previous decisions, we do not find the Army's practice of recording Stinger missile contracts at target price, rather than at ceiling price, to violate the Antideficiency Act. We would again caution that the Army should have employed certain safeguards, for example through reservations of funds, to avoid potential overobligation. As it happens, such safeguards were

unnecessary in the present case, as overobligations were avoided through contract modification.

Although administrative reservation of funds to cover contingent liabilities is not mandated by the Antideficiency Act, some obligation of funds to cover contingent liabilities may be required by 41 U.S.C. Sec. 114 (1976). ...

In reply we again stated that we would not object on Antideficiency Act grounds to the recording of fixed-price incentive contracts at target price. We warned, however, that this alone might not be sufficient to comply with the requirements of 41 U.S.C. Sec. 11 (1976). *Id.* at 8. *[Note: Content in 41 U.S.C. § 11 is now covered in 41 U.S.C. § 6301.]* We stated that current agency cost estimates would constitute an appropriate standard for determining the legality of contract actions in this context. Thus, we would find contract actions objectionable if, and to the extent that, such actions initiated during the fiscal year involved, "by current estimates, costs exceeding amounts presently available therefor." *Id.* at 9.

The standard of "current agency cost estimates" is one which we have articulated in later decisions. See, e.g., 55 Comp.Gen. 812, 824 (1976).

(GAO Decision B-206283)

...the recording of obligations under 31 U.S.C. § 200 *[now 1501]* is not the sole consideration in determining violations of 31 U.S.C. § 665 and 41 U.S.C. § 11. *[Note: Content in 41 U.S.C. § 11 is now covered in 41 U.S.C. § 6301.]* B-133170, *supra*; B-163058, *supra*.

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Wie [sic] believe that the words "any contract or other obligation" as used in 31 U.S.C. § 665 encompass not merely recorded obligations but other actions which give rise to Government liability and will ultimately require the expenditure of appropriated funds...

*(55 Comp .Gen. 812/GAO Decision B-184830)*

A fixed-price incentive contract is a fixed-price contract that provides for adjusting profit and establishing the final contract price by application of a formula based on the relationship of total final negotiated cost to total target cost. The final price is subject to a price ceiling, negotiated at the outset. The two forms of fixed-price incentive contracts, firm target and successive targets, are further described in 16.403-1 and 16.403-2 below.

*(FAR 16.403)*

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**Fully Funded Contract**

- A contract for which funds are obligated to cover the price or target price of a fixed-price contract or the estimated cost and any fee of a cost-reimbursement contract. Nonseverable contracts must be fully funded during the period of appropriation availability unless statutory authority allows incremental funding.

**CITATIONS:**

(a) If the contract is fully funded, funds are obligated to cover the price or target price of a fixed-price contract or the estimated cost and any fee of a cost-reimbursement contract.

*(FAR 32.703-1)*

Contracts that cannot be separated for performance by fiscal year may not be funded on an incremental basis without statutory authority. Such contracts, as "entire" or "nonseverable" under the bona fide need rule, are chargeable to the appropriation current at execution rather than funds current at the time goods or services are rendered.

*(GAO Decision B-241415)*

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**Grant or Cooperative Agreement**

- An instrument providing federal financial assistance in the form of an award, making payment in cash or in kind for a specified purpose. The federal government is not expected to have substantial involvement with the recipient while the contemplated activity is being performed. A cooperative agreement is similar to

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a grant with the exception that the federal government is expected to have substantial involvement.

Guidance and limitations concerning the funding of grants is found in 14 Code of Federal Regulations (CFR) 1260.11. In the grant context, the obligation occurs at the time of award.

For discretionary grants, record the full grant amount or amount to be funded in the current fiscal year as the obligation. For formula grants, record the amount determined by the formula or appropriation.

Consistent with NPR 5800.1E, NASA may award grants that contemplate financial assistance over several years. Traditional severability determinations do not apply in the grants context, and NASA has discretion to decide whether to fully or incrementally fund grant awards without regard to the nature of the work being supported.

NASA may fund any grant award fully at the time of award from an appropriation available for obligation at the time of award, even if the work will not be completed or funds disbursed until the period of availability has expired.

Additionally, NASA may incrementally fund multiple-year grant awards by using standard clauses from 14 CFR §§ 1260.52 and 1260.53 to limit NASA's obligation to fund grants up to a particular time period and/or amount (e.g., a fiscal year, or those funds available during the current year). These clauses indicate that NASA contemplates continuing financial assistance for future periods, but clearly states that additional funding is not guaranteed. When these clauses are properly used and invoked, exercise of each additional period of financial support is a new bona fide need, and funds from an appropriation current at the time of extension must be obligated. When incremental funding is used in this way, NASA personnel shall take care not to overtly or implicitly promise that continued financial support beyond the period or amount specified is guaranteed in any way.

#### CITATIONS:

If the amount of payment is under the control of the grantee, not the government, the government should obligate funds to cover its



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maximum potential liability.  
(GAO Decision B-300480.2)

For the reasons explained below, we conclude that (1) for grants, the principle of severability is irrelevant to a bona fide need determination, (2) a bona fide need analysis in the grant context focuses on whether the grants are made during the period of availability of the appropriation charged and further the authorized purposes of program legislation, (3) beginning in fiscal year 2002, Education's award of Early Childhood Educator program grants up to 4 years in duration is explicitly permitted by program authority and fulfills a bona fide need of the period for which the funds used are available, and (4) Education's award of 5-year GEAR UP grants during fiscal year 2001 and 2002 and 2-year Early Childhood Educator grants during fiscal year 2001 is in accordance with the program legislation and fulfills a bona fide need of the period for which the funds used are available...

The bona fide need rule is a fundamental principle of appropriations law addressing the availability as to time of an agency's appropriation. 73 Comp. Gen. 77, 79 (1994); 64 Comp. Gen. 410, 414-15 (1985). The rule establishes that an appropriation is available for obligation only to fulfill a genuine or bona fide need of the period of availability for which it was made.<sup>5</sup> 73 Comp. Gen. 77, 79 (1994). It applies to all federal government activities carried out with appropriated funds, including contract, grant, and cooperative agreement transactions.<sup>[6]</sup> 73 Comp. Gen. 77, 78-79 (1994). An agency's compliance with the bona fide need rule is measured at the time the agency incurs an obligation, and depends on the purpose of the transaction and the nature of the obligation being entered into. 61 Comp. Gen. 184, 186 (1981) (bona fide need determination depends upon the facts and circumstances of the particular case). In the grant context, the obligation occurs at the time of award.<sup>7</sup> 31 Comp. Gen. 608 (1952). See also 31 U.S.C. § 1501(a)(5)(B)...

[n. 6] The Grant and Cooperative Agreement Act of 1977, 31 U.S.C. §§ 6301-6308, requires the use of a procurement contract if the purpose of the transaction is to fund the agency's acquisition of property or services for its own needs. 31 U.S.C. § 6303. If the purpose is to provide assistance to a non-federal entity through the transfer of money or anything else of value to accomplish a public purpose, the proper funding mechanism is a grant. 31 U.S.C. §

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6304. If the assistance resembles a grant and substantial involvement is expected between the agency and the recipient when carrying out the contemplated activity, the proper funding mechanism is a cooperative agreement. 31 U.S.C. § 6305.

7 The particular obligating document may vary, and may even be in the form of an agency's approval of a grant application or a letter of commitment. See 39 Comp. Gen. 317 (1959); 37 Comp. Gen. 861, 863 (1958).]

We believe the application of the bona fide need rule found in the SBA case is the correct approach. It expressly recognizes the fundamental difference between a contract and a grant or cooperative agreement and the significance this difference has on a bona fide need analysis. Contracts and grants are transactions that fulfill significantly different needs of an agency, the former to acquire goods and services and the latter to provide financial assistance. B-222665, July 2, 1986 (principal purpose of a grant is to transfer something of value to the recipient to carry out a legislatively established public policy instead of acquiring goods or services for the direct benefit or use of the United States). See also 31 U.S.C. § 6303-4...

B-24827, April 3, 1942 (funds legally obligated at the time of grant agreement may be made available for expenditure without regard to the fiscal year limitation of obligated appropriation)...

see 73 Comp. Gen. 77 (1994) (bona fide need determination in the context of a cooperative agreement properly required assessing severability of research activities where agreement under which research was conducted more closely resembled a contract than a grant of financial assistance)...

When addressing compliance with the bona fide need rule for grants or cooperative agreements, the primary focus must be on the authority provided the agency.

*(GAO Decision B-289801)*

The Small Business Administration (SBA) asks several questions about application of the bona fide needs rule, 31 U.S.C. Sec. 1502(a), to its funding of certain Small Business Development Centers' (Centers) cooperative agreements on September 30 of a fiscal year, notwithstanding the fact that the services provided by

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the Centers will be performed in the subsequent fiscal year. The answer is that the rule is not violated. The agency's bona fide need is to provide assistance to Centers by entering into grants or cooperative agreements within the fiscal year sought to be charged.

...we do not think the September 30 fundings violate the bona fide needs rule...

(GAO Decision B-229873)

...In the context of discretionary grants, the obligation generally occurs at the time of award. *See, e.g.*, B-289801, Dec. 30, 2002; 31 Comp. Gen. 608 (1952).<sup>33</sup>

(Red Book, Chapter 10.C.2.b.)

## 20.5 When should I record obligations and in what amounts?

### (f) *Grants and fixed charges.*

Discretionary grants will be obligated after the amounts are determined administratively and recorded at the time the grant award is signed. The grant award is normally the documentary evidence that the grant has been awarded. Letters of credit are issued after the grant awards are made and generally are not obligating documents.

For grants and fixed charges with formulas in law that automatically fix the amount of the charges, record the amount determined by the formula or, if there is an appropriation, then record the amount appropriated, whichever is smaller. The obligation is reported at the time the grantee is awarded the grant and is liquidated when the payment is made to the grantee. To the extent that a grant awarded in a previous year is no longer valid, you will record a recovery of prior year obligations.

The exceptions follow:

Grants or fixed charges.	Amount obligated is...	At the time...
In lieu of taxes	The amount appropriated	The taxes are due.
Interest	The amount owed	The interest is payable.
Dividends	The amount	The dividend is

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declared

declared.

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*(OMB Circular No. A-11, Section 20.5)*

(g) 42 U.S.C. 2459d prohibits NASA from funding any grant for longer than one year if the effect is to provide a guaranteed customer base for new commercial space hardware or services. *[Note: Content in 42 U.S.C. § 2459d is now covered in 51 U.S.C. § 30301.]* The only exception would be if an Appropriations Act specifies the new commercial space hardware or services to be used.

(h) NASA reserves the right to either fully fund or incrementally fund grants based on fiscal law and program considerations. Incremental funding of grants and cooperative agreements shall conform to the following procedure: (1) When the period of performance for a grant crosses Government Fiscal Years, the grant will usually be incrementally funded, using appropriations from different Government Fiscal Years. In other circumstances, incremental funding may be appropriate. The special condition at 1260.53, Incremental Funding, will be included in any grant that is incrementally funded. The grant officer will determine the number of incremental funding actions that will be allowed.

(2) Specific limitations on incremental funding are as follows: (i) Grants that are funded using appropriations from different Government Fiscal Years should provide funding from the prior fiscal year that carries at least one month into the subsequent fiscal year in order to facilitate transition of the grant to the subsequent fiscal year's funding cycle.

(ii) Only those grants whose anticipated funding exceeds \$100,000 of appropriations from a single Government Fiscal Year may be incrementally funded within that fiscal year's appropriations.

(iii) Incremental funding actions to obligate or deobligate funds shall not total less than \$25,000 unless the action is necessary to comply with the requirement to use appropriations from different Government Fiscal Years, to fully fund a grant, to close out a grant, or to make a corrective accounting adjustment.

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(3) On an exception basis, and with the concurrence of the installation Chief Financial Officer (CFO) or Deputy CFO for Resources, the procurement officer may waive the restrictions set forth in paragraphs (h)(2)(i) through (h)(2)(iii) of this section for individual funding actions on individual grants. The procurement officer shall maintain a record of all such approvals during the fiscal year.

(4) The restrictions set forth in paragraphs (h)(2)(i) through (h)(2)(iii) of this section are not applicable during the period of a continuing resolution. During such a period, NASA will nonetheless endeavor to fund individual grants using reasonably sized increments.

*(14 CFR 1260.11, "Grant and Cooperative Agreement Handbook")*

The two recent decisions involving the Corporation for National and Community Service, discussed previously in section A of this chapter, held that the Corporation must record the government's full liability under the grant at the time of grant award. B-300480, Apr. 9, 2003, *aff'd*, B-300480.2, June 6, 2003. Under the grant agreements involved, the Corporation agreed to fund a specified number of AmeriCorps program participants. This number could be converted into a precise dollar amount. Thus, the Corporation incurred an obligation to pay the maximum dollar amount if the grantee fully performed under the grant agreement and enrolled the specified number of participants. While the grantee might ultimately fail to enroll the number of participants called for in the grant agreement, the extent of the grantee's performance under the grant was entirely within the grantee's control. The decisions rejected contentions by the Corporation and the Office of Management and Budget that the initial grant obligation should be recorded on the basis of estimates that reflected past experience. *(Red Book, Chapter 7.B.1.f.)*

("[DOL's] National emergency grant awards can be disbursed in a single payment or in increments. In most cases, the initial increment will be for 6 months to enable a project to achieve full enrollment. For grants disbursed in more than one payment, grantees are required to submit supplemental information along with their requests for future incremental payments. This

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information generally includes the actual number of participants, performance outcomes, and expenditures.”)  
(GAO-04-496)

A federal financial assistance award making payment in cash or in kind for a specified purpose. The federal government is not expected to have substantial involvement with the state or local government or other recipient while the contemplated activity is being performed. The term “grant” is used broadly and may include a grant to nongovernmental recipients as well as one to a state or local government, while the term “grant-in-aid” is commonly used to refer only to a grant to a state or local government.

(GAO’s “A Glossary of Terms Used in the Federal Budget Process”)

An executive agency shall use a grant agreement as the legal instrument reflecting a relationship between the United States Government and a State, a local government, or other recipient when—

- (1) the principal purpose of the relationship is to transfer a thing of value to the State or local government or other recipient to carry out a public purpose of support or stimulation authorized by a law of the United States instead of acquiring (by purchase, lease, or barter) property or services for the direct benefit or use of the United States Government; and
- (2) substantial involvement is not expected between the executive agency and the State, local government, or other recipient when carrying out the activity contemplated in the agreement.

(31 U.S.C. § 6304)

An executive agency shall use a cooperative agreement as the legal instrument reflecting a relationship between the United States Government and a State, a local government, or other recipient when—

- (1) the principal purpose of the relationship is to transfer a thing of value to the State, local government, or other recipient to carry out a public purpose of support or stimulation authorized by a law of the United States instead of acquiring (by purchase, lease, or

barter) property or services for the direct benefit or use of the United States Government; and

- (2) substantial involvement is expected between the executive

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agency and the State, local government, or other recipient when carrying out the activity contemplated in the agreement.  
(31 U.S.C. § 6305)

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**Incrementally  
Funded Contract**

- A contract in which the total work effort is performed over multiple time periods and funds are allotted to cover discernible phases or increments of performance. The term is generally used to refer to incremental funding in the budget on a year-by-year basis, but NASA also uses the term to refer to incrementally funding a contract or other procurement document within a single fiscal year.

**CITATIONS:**

An incrementally funded contract is a contract in which the total work effort is performed over multiple time periods and funds are allotted to cover discernible phases or increments of performance. This funding method allows for contracts to be awarded for periods in excess of one-year, even though the total estimated amount of funds to be obligated for the contract is not available at the time of contract award.

*(U.S. Army Corps of Engineers, Office of the Principal Assistant Responsible for Contracting (OPARC))*

Capital projects can be grouped into three funding categories: full funding, incremental funding, and high technology... High technology capital projects are incrementally funded projects for which budget authority is or appears to be provided for only part of the estimated cost of information technology acquisitions or projects that are highly dependent on research and development and highly uncertain in outcome. Space exploration equipment would be an example of such a project. Incremental funding can be justified for high technology capital projects because such projects are often closer in nature to research and development and funding provided on an incremental basis can provide useful knowledge even if no additional funding is provided...

*(GAO-01-432R)*

(b) If the contract is incrementally funded, funds are obligated to cover the amount allotted and any corresponding increment of fee.  
(FAR 32.703-1)

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**Indefinite Delivery,  
Indefinite Quantity**

- A form of an indefinite-delivery contract under which the government is required to order and the contractor required is to
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**(IDIQ)**

furnish a stated minimum quantity of supplies or services. The Government may place orders to meet its needs at any time during a fixed period.

The minimum contract amount is the obligation and must be funded by an appropriation available at the time of contract award. Amounts over the minimum are obligated as task or delivery orders are placed against the original contract. Current year funds are used when placing orders above the guaranteed minimum. Although the period for ordering under an IDIQ contract may extend beyond the appropriation's period of availability, the minimum requirement and each task order placed must conform to PIC 11-05 performance period requirements.

**CITATIONS:**

CONTRACTS WHICH AUTHORIZE VARIATIONS IN THE DELIVERY QUANTITIES SHOULD BE RECORDED AS OBLIGATIONS UNDER SECTION 1311 OF THE SUPPLEMENTAL APPROPRIATION ACT, 1955, FOR THE PRICE OF THE QUANTITY SPECIFIED FOR DELIVERY, EXCLUSIVE OF THE PERMITTED VARIATIONS; HOWEVER, IN ORDER TO PREVENT VIOLATIONS OF THE ANTI-DEFICIENCY ACT, SUFFICIENT FUNDS SHOULD BE RESERVED TO COVER THE EXCESS OF THE ESTIMATED INCREASES OVER DECREASES.

*(34 Comp. Gen. 418/GAO Decision B-121982)*

From an appropriations standpoint, an agency must record an obligation against its appropriation at the time that it incurs a legal liability, such as when the agency signs a contract committing the government to purchase a specified amount of goods or services. B-116795, June 18, 1954. *See also* B-300480.2, June 6, 2003, at 3 n.1. In the case of an IDIQ contract, the agency must record an obligation in the amount of the guaranteed minimum at the time the contract is executed because, at that point, the government has a fixed liability for the minimum amount to which it committed itself. B-308969, May 31, 2007; B-302358, Dec. 27, 2004. A valid obligation must reflect a *bona fide* need at the time the obligation is incurred. Thus the agency must have a *bona fide* need for the guaranteed minimum. *See* B-317636, Apr. 21, 2009; B-308969, May 31, 2007...



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*(GAO Decision B-318046)*

...An agency must record an obligation against its appropriation at the time that it incurs a legal liability for payment from that appropriation. B-300480.2, June 6, 2003; B-300480, Apr. 9, 2003; 42 Comp. Gen. 733, 734 (1963). Clearly, an agency can incur a legal liability, that is, a claim that may be legally enforced against the government, by signing a contract. B-300480.2, June 6, 2003. We addressed the question of the proper obligation of an IDIQ contract in our decision, B-302358, Dec. 27, 2004:

“When an agency executes an indefinite-quantity contract such as an IDIQ contract, the agency must record an obligation in the amount of the required minimum purchase. . . . At the time of award, the government has a fixed liability for the minimum amount to which it committed itself. See [Federal Acquisition Regulation] 16.504(a)(1) (specifying that an IDIQ contract must require the agency to order a stated minimum quantity). An agency is required to record an obligation at the time it incurs a legal liability. 65 Comp. Gen. 4, 6 (1985); B-242974.6, Nov. 26, 1991. Therefore, for an IDIQ contract, an agency must record an obligation for the minimum amount at the time of contract execution.

“Further obligations occur as task or delivery orders are placed and are chargeable to the fiscal year in which the order is placed.”

Thus, in the case of an IDIQ contract, the government incurs a legal liability in the amount of the guaranteed minimum at the time at which it awards the contract.

*(GAO Decision B-308969)*

Contract clause, I.13, entitled “Indefinite Quantity,” [5] further supports our conclusion that SWB incurred an obligation at the time of contract award. It provides, in part (with emphasis added):

“This is an indefinite-quantity contract for the supplies or services specified, and effective for the period stated, in the Schedule. . . . The Contractor shall furnish

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to the Government, when and if ordered, the supplies or services specified in the Schedule up to and including the quantity designated in the Schedule as the ‘maximum’. The Government shall order at least the quantity of supplies or services designated in the Schedule as the ‘minimum’.”

By using the words “shall order,” the emphasized sentence indicates that under the contract the government is liable to the contractor for the minimum specified in the contract. It therefore incurs a legal liability for that amount. This is so whether SWB ever issues a task order to the contractor or not, and is so immediately upon contract award...

[n. 5] Federal Acquisition Regulation (FAR), 48 C.F.R. § 52.216-22.

*(GAO Decision B-308969)*

## DIGEST

1. Customs's Automated Commercial Environment (ACE) contract was an indefinite delivery, indefinite quantity (IDIQ) contract and therefore was not subject to the multiyear contracting requirements of 41 U.S.C. 254c, including the termination provisions in that section. *[Note: Content covered in 41 U.S.C. § 254c is now covered in 41 U.S.C. § 3903.]*

2. Upon award of Automated Commercial Environment (ACE) contract, Customs should have obligated the contract minimum of 25 million in accordance with 31U.S.C. 1501(a), the recording statute, to ensure the integrity of Customs's obligational accounting records.

*(GAO Decision B-302358)*

*An indefinite-quantity contract* is one in which the contractor agrees to supply whatever quantity the government may order, within limits, with the government under no obligation to use that contractor for all of its requirements.

*(Red Book, Chapter 7.B.1.e.)*

...for many types of obligations, the precise amount of the government’s liability cannot be known at the time the liability is

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incurred. As summarized in our preliminary discussion of 31 U.S.C. § 1501(a), some initial amount must still be recorded. The agency should then adjust this initial obligation amount up or down periodically as more precise information becomes available.[12]

GAO decisions, as well as GAO's *Policy and Procedures Manual for Guidance of Federal Agencies*, indicate that, in general, the agency should use its best estimate to record the initial amount where the amount of the government's final liability is undefined. *E.g.*, 56 Comp. Gen. 414, 418 (1977); 50 Comp. Gen. 589 (1971). Section 3.5.D of the *Manual* further provides that, where an estimate is used, the basis for the estimate and the computation must be documented...

[n.12 This discussion addresses the amount to be recorded when the amount of the liability is undefined, and is not to be confused with a discussion of contingent liabilities. For example, for an indefinite-delivery, indefinite-quantity contract, any liability in excess of the government's minimum commitment, as defined in the contract, is a contingent liability—that is, contingent on the government placing future orders with the contractor. For that reason, at the time the government enters into the contract, the government has no liability above the minimum specified in the contract, and thus incurs no obligation for future orders.]

(*Red Book*, Chapter 7.B.1.f.)

#### **16.501-2 General.**

(a) There are three types of indefinite-delivery contracts: definite-quantity contracts, requirements contracts, and indefinite-quantity contracts. . . .

#### **16.502 Definite-quantity contracts.**

(a) *Description.* A definite-quantity contract provides for delivery of a definite quantity of specific supplies or services for a fixed period, with deliveries or performance to be scheduled at designated locations upon order.

#### **16.503 Requirements contracts.**

(a) *Description.* A requirements contract provides for filling all actual purchase requirements of designated Government activities for supplies or services during a specified contract period, with

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deliveries or performance to be scheduled by placing orders with the contractor.

**16.504 Indefinite-quantity contracts.**

(a) *Description.* An indefinite-quantity contract provides for an indefinite quantity, within stated limits, of supplies or services during a fixed period. The Government places orders for individual requirements. Quantity limits may be stated as number of units or as dollar values.

(1) The contract must require the Government to order and the contractor to furnish at least a stated minimum quantity of supplies or services. In addition, if ordered, the contractor must furnish any additional quantities, not to exceed the stated maximum. The contracting officer should establish a reasonable maximum quantity based on market research, trends on recent contracts for similar supplies or services, survey of potential users, or any other rational basis.

(2) To ensure that the contract is binding, the minimum quantity must be more than a nominal quantity, but it should not exceed the amount that the Government is fairly certain to order.

(FAR 16.501-504)

32.703-2 Contracts conditioned upon availability of funds...

(b) *Indefinite-quantity or requirements contracts.* A one-year indefinite-quantity or requirements contract for services that is funded by annual appropriations may extend beyond the fiscal year in which it begins; provided, that—

(1) Any specified minimum quantities are certain to be ordered in the initial fiscal year (see 37.106) and

(2) The contract includes the clause at 52.232-19, Availability of Funds for the Next Fiscal Year (see 32.705-1(b)).

(FAR 32.703-2b.)

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**Land and Structures** — Record contracts for lands and structures according to the guidelines under Contracts, except as provided in OMB Circular No. A-11.

**20.5 When should I record obligations and in what amounts?**

(e) *Land and structures.*

Contracts for lands and structures generally follow the same rules as for contracts specified above with the following exceptions.

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Contracts with...	Amount obligated is...	At the time ...
Condemnation proceedings	The estimated amount for the price of the land, adjusted to the amount of the payment to be held in escrow where there is a declaration of taking	When you ask the Attorney General to start condemnation proceedings.
Lease-purchases and capital leases covered by the scorekeeping rules developed under the Budget Enforcement Act	<p>The present value of the lease payments, discounted using the Treasury interest rate used in calculating the budget authority provided for the purchase</p> <p>The imputed interest costs (that is, the financing costs Treasury would have incurred if it had issued the debt to acquire the asset)</p>	<p>The contract is signed.</p> <p>During the lease period.</p>

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*(OMB Circular No. A-11, Section 20.5)*

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<b>Letter Contract</b>	—	<p>A letter contract is a written preliminary contractual instrument that authorizes the contractor to begin immediately manufacturing supplies or performing services.</p> <p>The obligation is the maximum liability under the contract itself. If a contract is definitized in the following fiscal year, the</p>
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obligation that must be funded by an appropriation current at the time the letter contract is awarded is the amount of the definitized contract minus either (a) actual costs incurred under the letter contract (when known), or (b) the maximum legal liability stated in the letter contract (when the actual costs cannot be determined). The remaining amount to be recorded is obligated against the appropriation current at the time of definitization.

CITATIONS:

LETTER CONTRACTS, LETTERS OF INTENT, AND AMENDMENTS SHOULD BE RECORDED AS OBLIGATIONS PURSUANT TO SECTION 1311 OF THE SUPPLEMENTAL APPROPRIATION ACT, 1955, AT THE MAXIMUM LIABILITY NECESSARY TO COVER EXPENSES INCURRED BY THE CONTRACTOR PRIOR TO THE EXECUTION OF A DEFINITIVE CONTRACT...  
(34 Comp. Gen. 418/GAO Decision B-121982)

Where a letter contract and the subsequent superseding agreement are entered into during the same fiscal year, the cost of both contracts is obligated against the same fiscal year appropriation. However, when the letter contract is entered into during one year and the superseding agreement is not definitized until the next fiscal year, then it is appropriate to obligate only the maximum liability which may be incurred under the letter contract against appropriations current when it is entered into. The superseding contract is obligated against appropriations current when it is definitized and entered into...

The amount of the definitized contract would ordinarily be the total contract cost less either the actual costs incurred under the letter contract (when known) or the amount of the maximum legal liability permitted by the letter contract (when the actual costs cannot be determined). 2/

[n. 2/ See 31 U.S.C. § 1501]

(GAO Decision B-197274)

A letter of intent which amounts to a contract is also called a "letter contract." In the context of government procurement, it is used most commonly when there is insufficient time to prepare

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and execute the full contract before the end of the fiscal year. As indicated in the legislative history quoted earlier, a “letter of intent” accepted by the contractor may form the basis of an obligation if it is sufficiently specific and definitive to show the purpose and scope of the contract. 21 Comp. Gen. 574 (1941); B-127518, May 10, 1956. Letters of intent should be used “only under conditions of the utmost urgency.” 33 Comp. Gen. 291, 293 (1954). Under the Federal Acquisition Regulation (FAR), letter contracts may be used—

“when (1) the Government’s interests demand that the contractor be given a binding commitment so that work can start immediately and (2) negotiating a definitive contract is not possible in sufficient time to meet the requirement. However, a letter contract should be as complete and definite as feasible under the circumstances.”

48 C.F.R. § 16.603-2(a) (2005).

The amount to be obligated under a letter contract is the government’s maximum liability under the letter contract itself, without regard to additional obligations anticipated to be included in the definitive contract or, restated, the amount necessary to cover expenses to be incurred by the contractor prior to execution of the definitive contract. The obligation is recorded against funds available for obligation at the time the letter contract is issued. 34 Comp. Gen. 418, 421 (1955); B-197274, Sept. 23, 1983; B-197274, Feb. 16, 1982; B-127518, May 10, 1956. *See also* FAR, 48 C.F.R. §§ 16.603-2(d), 16.603-3(a).

Once the definitive contract is executed, the government’s liability under the letter contract is merged into it. If definitization does not occur until the following fiscal year, the definitive contract will obligate funds of the latter year, usually in the amount of the total contract price less an appropriate deduction relating to the letter contract. B-197274, Sept. 23, 1983. The cited decision, at page 5, specifies how to calculate the deduction as follows:

“The definitized contract then supports obligating against the appropriation current at the time it is entered into since it is, in fact, a *bona fide* need of that year. The amount of the definitized contract would ordinarily be the total contract cost less either the actual costs incurred under the

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letter contract (when known) or the amount of the maximum legal liability permitted by the letter contract (when the actual costs cannot be determined).”

Letter contracts should be definitized within 180 days, or before completion of 40 percent of the work to be performed, whichever occurs first. FAR, 48 C.F.R. § 16.603-2(c). Also, letter contracts should not be used to record excess obligations as this distorts the agency’s funding picture. *See* GAO, *Contract Pricing: Obligations Exceed Definitized Prices on Unpriced Contracts*, GAO/NSIAD-86-128 (Washington, D.C.: May 2, 1986).

*(Red Book, Chapter 7.B.1.a.)*

A letter contract is a written preliminary contractual instrument that authorizes the contractor to begin immediately manufacturing supplies or performing services.  
*(FAR 16.603-1)*

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**Multiyear Contract**

- A contract covering the needs or requirements of more than one fiscal year without establishing and having to exercise an option for each program year after the first. The multiyear contract may cover no more than five program years. 10 U.S.C. § 2306b and 2306c set forth the criteria that NASA’s multiyear contracts must meet, and GAO’s Red Book provide the following example to help in determining whether a contract is or is not “multiyear”: “A contract for the needs of the current year, even though performance may extend over several years, is not a multiyear contract... Thus, a contract to construct a ship that will take 3 years to complete is not a multiyear contract; a contract to construct one ship a year for the next 3 years is.” Multiyear contracts having cancellation ceilings exceeding \$100,000,000 have Congressional notification requirements before award. Multiyear contracting authority is not generally used at NASA.

Record an obligation for: (1) the entire amount of the 5-year contract against the fiscal year appropriation current at the time of contract award plus termination costs; or (2) the amount for each of the 5 years against appropriations enacted for each of those years when the funds have been appropriated.

**CITATIONS:**



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"Multi-year contract" means a contract for the purchase of supplies or services for more than 1, but not more than 5, program years. A multi-year contract may provide that performance under the contract during the second and subsequent years of the contract is contingent upon the appropriation of funds, and (if it does so provide) may provide for a cancellation payment to be made to the contractor if appropriations are not made. The key distinguishing difference between multi-year contracts and multiple year contracts is that multi-year contracts, defined in the statutes cited at 17.101, buy more than 1 year's requirement (of a product or service) without establishing and having to exercise an option for each program year after the first.  
(FAR 17.103)

A multiyear contract, as we use the term in this discussion, is a contract covering the requirements, or needs, of more than one fiscal year. A contract for the needs of the current year, even though performance may extend over several years, is not a multiyear contract. We discuss contracts such as these, where performance may extend beyond the end of the fiscal year, in sections B.4 and B.5 of this chapter. Thus, a contract to construct a ship that will take 3 years to complete is not a multiyear contract; a contract to construct one ship a year for the next 3 years is.  
(Red Book, Chapter 5.B.8.a.)

Sections 2306b and 2306c permit the military departments to obligate the entire amount of the 5-year contract to the fiscal year appropriation current at the time of contract award, even though the goods or services procured for the final 4 years of the contract do not constitute needs of that fiscal year. Alternatively, sections 2306b and 2306c permit the military departments to obligate the amount for each of the 5 years against appropriations enacted for each of those years. If funds are not made available for continuation in a subsequent fiscal year, cancellation or termination costs may be paid from appropriations originally available for the contract, appropriations currently available for the same general purpose, or appropriations made specifically for those payments. 10 U.S.C. §§ 2306b(f) and 2306c(e). The authority contained in sections 2306b and 2306c is also available to the Coast Guard and the National Aeronautics and Space Administration. 10 U.S.C. § 2303... A contract under sections 2306b or 2306c must relate to the *bona fide* needs of the contract period as opposed to the need

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only of the first fiscal year of the contract period. The statute does not authorize the advance procurement of materials not needed during the 5-year term of the contract. *See* 64 Comp. Gen. 163 (1984); B-215825-O.M., Nov. 7, 1984. *See also* 35 Comp. Gen. 220 (1955)...

*(Red Book, Chapter 5.B.9.b.(1))*

**(a) In General.**— To the extent that funds are otherwise available for obligation, the head of an agency may enter into multiyear contracts for the purchase of property whenever the head of that agency finds each of the following:

(1) That the use of such a contract will result in substantial savings of the total anticipated costs of carrying out the program through annual contracts.

(2) That the minimum need for the property to be purchased is expected to remain substantially unchanged during the contemplated contract period in terms of production rate, procurement rate, and total quantities.

(3) That there is a reasonable expectation that throughout the contemplated contract period the head of the agency will request funding for the contract at the level required to avoid contract cancellation.

(4) That there is a stable design for the property to be acquired and that the technical risks associated with such property are not excessive.

(5) That the estimates of both the cost of the contract and the anticipated cost avoidance through the use of a multiyear contract are realistic.

(6) In the case of a purchase by the Department of Defense, that the use of such a contract will promote the national security of the United States.

(7) In the case of a contract in an amount equal to or greater than \$500,000,000, that the conditions required by subparagraphs (C) through (F) of paragraph (1) of subsection (i) will be met, in accordance with the Secretary's certification and determination under such subsection, by such contract. ///

**(k) Multiyear Contract Defined.**— For the purposes of this section, a multiyear contract is a contract for the purchase of property for more than one, but not more than five, program years. *(10 U.S.C. § 2306b)*

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**(a) Authority.**— Subject to subsections (d) and (e), the head of an agency may enter into contracts for periods of not more than five years for services described in subsection (b), and for items of supply related to such services, for which funds would otherwise be available for obligation only within the fiscal year for which appropriated whenever the head of the agency finds that—

- (1) there will be a continuing requirement for the services consonant with current plans for the proposed contract period;
- (2) the furnishing of such services will require a substantial initial investment in plant or equipment, or the incurrence of substantial contingent liabilities for the assembly, training, or transportation of a specialized work force; and
- (3) the use of such a contract will promote the best interests of the United States by encouraging effective competition and promoting economies in operation.

**(b) Covered Services.**— The authority under subsection (a) applies to the following types of services:

- (1) Operation, maintenance, and support of facilities and installations.
- (2) Maintenance or modification of aircraft, ships, vehicles, and other highly complex military equipment.
- (3) Specialized training necessitating high quality instructor skills (for example, pilot and air crew members; foreign language training).
- (4) Base services (for example, ground maintenance; in-plane refueling; bus transportation; refuse collection and disposal).
- (5) Environmental remediation services for—
  - (A) an active military installation;
  - (B) a military installation being closed or realigned under a base closure law; or
  - (C) a site formerly used by the Department of Defense...

**(f) Multiyear Contract Defined.**— For the purposes of this section, a multiyear contract is a contract for the purchase of services for more than one, but not more than five, program years. Such a contract may provide that performance under the contract during the second and subsequent years of the contract is contingent upon the appropriation of funds and (if it does so provide) may provide for a cancellation payment to be made to the contractor if such appropriations are not made.

*(10 U.S.C. § 2306c.)*

Multiyear contracting is a special authority for acquiring more than

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one year's requirements—including weapon systems— under a single contract award without having to exercise an option for each program year after the first.  
( *GAO-08-298*)

Additional discussion.  
(*Red Book, Chapter 6.C.2.b.(4)*)

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**Nonseverable  
(Entire) Service**  
(*see also  
Severable Service*)

- A service that, by its nature, cannot be separated for performance in separate fiscal years. The service involves work which cannot be separated into components, but constitutes a specific, entire job with a defined end product that must be performed as a single task to meet a need of the government.

The entire contract or task order price must be obligated using an appropriation available for obligation at time of award, notwithstanding that performance may extend into future fiscal years. A limitation of funds clause does not affect the applicable bona fide needs rule or the severable test.

**CITATIONS:**

“Nonseverable services” – services which constitute a specific, entire job with a defined endproduct that cannot feasibly be subdivided for separate performance in each fiscal year, essentially a single undertaking which, by its nature, cannot be separated for performance in separate fiscal years. Contracts for nonseverable services should be financed entirely out of the appropriation current at the time of award, notwithstanding that performance may extend into future years. Examples of nonseverable services are studies, reports, overhaul of an engine, painting a building, etc.  
(*Uscourts.gov's JP3 Glossary of Terms*)

The Comptroller General has held that the question of whether to charge the appropriation current on the date the contract is made, or to charge funds current at the time the services are rendered, depends upon whether the services are “severable” or “entire”... A contract that is viewed as “entire” is chargeable to the fiscal year in which it was made, notwithstanding that performance may have extended into the following fiscal year. The determining factor for whether services are severable or entire is whether they represent a single undertaking...  
...(subsequent modifications to Fish and Wildlife Service research

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work orders should be charged to the fiscal year current when the work orders were issued since the purpose of the research is to provide a final research report and the services under the contract are nonseverable). The last opinion is noteworthy because it pointed out that a limitation of funds clause does not affect the application of the *bona fide* needs rule and the severable test. 73 Comp. Gen. at 80...

Training tends to be nonseverable. Thus, where a training obligation is incurred in one fiscal year, the entire cost is chargeable to that year, regardless of the fact that performance may extend into the following year.

(*Red Book, Chapter 5.B.5.*)

[W]here the services provided constitute a specific, entire job with a defined end-product that cannot feasibly be subdivided for separate performance in each fiscal year, the task should be financed entirely out of the appropriation current at the time of award, notwithstanding that performance may extend into future fiscal years. See 71 Comp. Gen. 428. The bona fide need rule allows time-limited funds to be used for work performed in the next fiscal period in connection with a nonseverable task since the latter effort is viewed as an inseparable continuation of work to fulfill a need that arose during the appropriation's period of availability. (*GAO Decision B-240264*)

A non-severable task, on the other hand, involves work which cannot be separated into components, but instead must be performed as a single task to meet a need of the government. See 60 Comp. Gen., *supra*. It follows, then, that the bona fide need rule does not preclude using time-limited funds for work performed in the next fiscal period in connection with a non-severable task, since the later effort is viewed as an inseparable continuation of work to fulfill a need that arose during the appropriation's period of availability.

(*GAO Decision B-235678*)

However, a need may arise in one fiscal year for services which, by their nature, cannot be separated for performance in separate fiscal years. *Id.* The question whether to charge the appropriation current on the date of contract award or to charge the appropriation current on the date the services are rendered turns on whether the services are "severable" or "nonseverable" (or "entire"). *Id.*; see

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65 Comp. Gen. at 743. A severable service is one in which the government receives value as the service is rendered. A nonseverable or entire service is one in which the government receives value only when the entire service has been performed. (GAO Decision B-257977)

For service contracts, whether an expense was properly incurred or properly made during the period of availability depends upon whether the services are severable or nonseverable. A nonseverable contract is essentially a single undertaking that cannot be feasibly subdivided. B-240264, Feb. 7, 1994. It is considered a bona fide need of the fiscal year in which the agency entered into the contract. Consequently, agencies should record nonseverable service contracts as obligations at the time of award. (GAO Decision B-259274)

Contracts that cannot be separated for performance by fiscal year may not be funded on an incremental basis without statutory authority. Such contracts, as "entire" or "nonseverable" under the bona fide need rule, are chargeable to the appropriation current at execution rather than funds current at the time goods or services are rendered. (GAO Decision B-241415)

A task is severable if it can be separated into components that independently meet a separate and ongoing need of the government.<sup>6</sup> Thus to the extent that a need for a specific portion of a continuing service arises in a subsequent fiscal year, that portion is severable and chargeable to appropriations available in the subsequent fiscal year. 60 Comp. Gen. 219, 220-221 (1981). However, where the service provided constitutes a specific, entire job with a defined end-product that cannot feasibly be subdivided for separate performance in each fiscal year, the task should be financed entirely out of the appropriation current at the time of award, notwithstanding that performance may extend into future years. B-240264, February 7, 1994. Thus a nonseverable contract is essentially a single undertaking that cannot feasibly be subdivided. B-259274, May 22, 1996. Whether the subdivision is feasible or not is a matter of judgment that includes as a minimum a determination of whether the government has received value from the service rendered. 58 Comp. Gen. 321 (1979). These general rules apply to all fixed period appropriations, whether for one year

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or three years. 65 Comp. Gen. 170, 171 (1989).  
(GAO Decision B-277165)

3. *Nonseverable Services*:

- a. A service is nonseverable if the service produces a single or unified outcome, product, or report that cannot be subdivided for separate performance in different fiscal years.
- b. For nonseverable contracts, the government must fund the entire effort with dollars available for obligation at the time the contract is executed, and the contract performance may cross fiscal years. (79th Fiscal Law Course Deskbook, Chapter 3.IV.F.3.)

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**Ordering  
Agreement**

- A basic ordering agreement is a written instrument of understanding, negotiated between an agency and a contractor, that contains (1) terms and clauses applying to future contracts (orders) between the parties during its term, (2) a description, as specific as practicable, of supplies or services to be provided, and (3) methods for pricing, issuing, and delivering future orders under the basic ordering agreement. A basic ordering agreement is not a contract.

The obligation is incurred when an order is placed under the ordering agreement.

CITATIONS:

Basic ordering agreements (BOAs) are essentially open-ended agreements between a government agency and a contractor against which specific orders for specific items and services may be placed. FAR sect. 16.703. BOAs are often used when the specific items and quantities to be covered by a contract are not known at the time the agreement is executed. B-244633, Nov. 6, 1991, at 3 n.3... BOAs are not contracts, and the government is not required to place any orders under these agreements. *Id.* Thus, placement of an order (and acceptance by the contractor), consistent with the FAR and the terms of the BOA, is the point at which there is a binding commitment which creates a legal liability of the government for the payment of appropriated funds for the goods or services ordered and the government incurs an obligation that must be recorded against the proper appropriation. 31 U.S.C. sect. 1501(a)(1). No obligation is incurred when the agency and contractor enter into a BOA.  
(GAO Decision B-318046)



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(a) *Description.* A basic ordering agreement is a written instrument of understanding, negotiated between an agency, contracting activity, or contracting office and a contractor, that contains (1) terms and clauses applying to future contracts (orders) between the parties during its term, (2) a description, as specific as practicable, of supplies or services to be provided, and (3) methods for pricing, issuing, and delivering future orders under the basic ordering agreement. A basic ordering agreement is not a contract.  
(FAR 16.703)

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**Requirements  
Contract**

- A requirements contract provides for filling all actual purchase requirements of designated Government activities for supplies or services during a specified contract period, with deliveries or performance to be scheduled by placing orders with the contractor.

The obligation is incurred when an order for goods or services is placed against the requirements contract.

**CITATIONS:**

Unlike the IDIQ contract, no minimum guarantees are required for a requirements contract because the agreement to procure all of the agency's requirements constitutes adequate consideration for the contract. 50 Comp. Gen. 506, 508 (1971); B-213046, Dec. 27, 1983. Since there is no guaranteed minimum, the government does not incur an obligation until an order for goods or services is placed against the requirements contract. B-302358, Dec. 27, 2004; B-259274, May 22, 1996.  
(GAO Decision B-318046)

*A requirements contract* is one in which the government agrees to purchase all of its needs for the particular item or service during the contract period from the contractor, and the contractor agrees to fill all such needs...  
(Red Book, Chapter 7.B.1.e.)

(a) *Description.* A requirements contract provides for filling all actual purchase requirements of designated Government activities for supplies or services during a specified contract period, with deliveries or performance to be scheduled by placing orders with the contractor.

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**Research and Development (R&D)**

- The collection of efforts directed toward gaining greater knowledge or understanding and applying knowledge toward the production of useful materials, devices, and methods. These activities comprise creative work undertaken on a systematic basis to increase knowledge and the use of this knowledge to devise new applications. OMB defines R&D as including basic research, applied research, development, R&D equipment, and R&D facilities.

More detailed definitions for the above terms are found in OMB Circular No. A-11, Section 84 (provided under Citations below). Definitions specifically related to NASA research and technology and technology development programs and projects are found in NPR 7120.8, and those related to space flight projects are found in NPR 7120.5.

For funding guidance on R&D and technology development contracts, see “R&D/Technology Development Contracts” below.

**CITATIONS:**

R&D is the collection of efforts directed toward gaining greater knowledge or understanding and applying knowledge toward the production of useful materials, devices, and methods. R&D investments can be characterized as basic research, applied research, development, R&D equipment, or R&D facilities. The Office of Management and Budget has used those or similar categories in its collection of R&D data since 1949.  
*(President’s Budget of the United States, Fiscal Year 2012, Analytical Perspectives, 22. Research and Development)*

Research and development facilities: Amounts for the construction and rehabilitation of research and development facilities. Includes the acquisition, design, and construction of, or major repairs or alterations to, all physical facilities for use in R&D activities. Facilities include land, buildings, and fixed capital equipment, regardless of whether the facilities are to be used by the Government or by a private organization, and regardless of where title to the property may rest. Includes the international space station and such fixed facilities as reactors, wind tunnels, and

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particle accelerators...

Research and development equipment: Amounts for major equipment for research and development. (See category 14xx for the definition of research and development.) Includes acquisition or design and production of movable equipment, such as spectrometers, research satellites, detectors, and other instruments. At a minimum, this line should include programs devoted to the purchase or construction of R&D equipment

Conduct of research and development: Research and development (R&D) activities comprise creative work undertaken on a systematic basis in order to increase the stock of knowledge, including knowledge of man, culture and society, and the use of this stock of knowledge to devise new applications...

Basic research is defined as systematic study directed toward fuller knowledge or understanding of the fundamental aspects of phenomena and of observable facts without specific applications towards processes or products in mind...

Applied research is defined as systematic study to gain knowledge or understanding necessary to determine the means by which a recognized and specific need may be met...

Development is defined as systematic application of knowledge or understanding, directed toward the production of useful materials, devices, and systems or methods, including design, development, and improvement of prototypes and new processes to meet specific requirements.

*(OMB Circular No. A-11, Section 84)*

“Basic research” means that research directed toward increasing knowledge in science. The primary aim of basic research is a fuller knowledge or understanding of the subject under study, rather than any practical application of that knowledge.  
*(FAR 2.101)*

(b) In basic research the emphasis is on achieving specified objectives and knowledge rather than on achieving predetermined end results prescribed in a statement of specific performance characteristics. This emphasis applies particularly during the early

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or conceptual phases of the R&D effort.  
(FAR 35.005)

“Applied research” means the effort that (a) normally follows basic research, but may not be severable from the related basic research; (b) attempts to determine and exploit the potential of scientific discoveries or improvements in technology, materials, processes, methods, devices, or techniques; and (c) attempts to advance the state of the art. When being used by contractors in cost principle applications, this term does not include efforts whose principal aim is the design, development, or testing of specific items or services to be considered for sale; these efforts are within the definition of “development,” given below.

“Development,” as used in this part, means the systematic use of scientific and technical knowledge in the design, development, testing, or evaluation of a potential new product or service (or of an improvement in an existing product or service) to meet specific performance requirements or objectives. It includes the functions of design engineering, prototyping, and engineering testing; it excludes subcontracted technical effort that is for the sole purpose of developing an additional source for an existing product...

(FAR 35.001)

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**R&D/Technology  
Development  
Contracts**

- The primary purpose of contracted R&D programs is to advance scientific and technical knowledge and apply that knowledge to the extent necessary to achieve agency and national goals. Unlike contracts for supplies and services, most R&D contracts are directed toward objectives for which the work or methods cannot be precisely described in advance. It is difficult to judge the probabilities of success or required effort for technical approaches, some of which offer little or no early assurance of full success.

Technology development, or high technology, projects are close in nature to research and development, even though they are intended to produce end items. They are highly dependent on R&D and highly uncertain in outcome.

NASA’s R&D and technology development contracts may be fully or incrementally funded if a review by OGC, Office of Procurement and OCFO at an Acquisition Strategy Meeting (ASM) or Procurement Strategy Meeting (PSM) affirms that the planned

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contract/task order(s) are for R&D or technology development activities. For requirements that do not require an ASM or PSM, Center OGC, Procurement, and OCFO must conduct a review as early in the acquisition cycle as practicable.

When incrementally funding R&D and high technology projects, the contract must make clear that the Government's obligation is strictly limited to the amount of funding obligated and that no additional work may be performed on behalf of the Government unless and until the contract is modified to authorize further funding. The period of performance for a contract for R&D or technology development activities, or delivery date for R&D hardware items, may extend beyond the period of funding availability, as long as the appropriate contract language limiting the Government's obligation is used.

Contracts for activities that are in support of R&D or technology development that have minimal or no R&D or technology development must undergo a severability determination to determine the contract funding requirements. (See Nonseverable Service, Severable Service, and Severable Test.)

#### CITATIONS:

- R&D and technology development requirements and their contracts may continue to be either fully or incrementally funded if a review by OGC, OP, and OCFO at an Acquisition Strategy Meeting or Procurement Strategy Meeting affirms that the planned contract/task order(s) are for R&D or technology development activities<sup>1</sup>. For requirements determined at a level below that presented at an ASM or PSM, Center OGC, OP, and OCFO must conduct the review as early in the acquisition cycle as practicable. Furthermore, the period of performance for a contract for R&D or technology development activities, or delivery date for R&D hardware items, may extend beyond the period of funding availability<sup>2</sup>, as long as the contract language discussed below are inserted into the contract.
- Every requirement, activity, program or project that NASA executes by contract is not R&D or technology development activity. Moreover, some requirements in support of R&D and

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technology development programs have minimal or no R&D or technology development content. Therefore, non-R&D and non-technology development requirements/programs/projects/activities must undergo a severability determination process. It is important to review requirements with Center or Headquarters OGC, OCFO, and OP to make severability or other funding determinations as early in the acquisition process as practicable to ensure the bona fide need requirement is met.

- Effective immediately, ASMs will include a review of the Mission Directorate's requirements portfolio and make a determination as to whether or not the requirements, including any anticipated options, meet the requirements of this memo. Additionally, PSMs will include a review of the planned contract requirements, including any anticipated options, to make a determination as to whether or not these meet the requirements of this memo.

<sup>1</sup> The Office of Management and Budget defines R&D as including basic research, applied research, development, R&D equipment, and R&D facilities. *President's Budget of the United States, Fiscal Year 2012, Analytical Perspectives*, 22. *Research and Development*: "R&D is the collection of efforts directed toward gaining greater knowledge or understanding and applying knowledge toward the production of useful materials, devices, and methods. R&D investments can be characterized as basic research, applied research, development, R&D equipment, or R&D facilities." Technology development, or high technology projects, are highly dependent on R&D and uncertain in outcome. *See GAO 01-432R*.

<sup>2</sup> "There is no bar in Part 35 of the FAR against R&D contracts extending beyond 5 years. Nor are we aware of any FAR provision limiting an R&D contract such as this to a duration of 5 years, and GAO has acknowledged that R&D programs "must be continued over many years if they are to produce the end product." Report by the Comptroller General, Multiyear Authorizations for Research and Development, PAD-81-61, B-202294 (June 1981).

(NASA OCFO Decision Memorandum 12-02: Funding for

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*Research and Development (R&D) and Technology Development Contracts)*

The primary purpose of contracted R&D programs is to advance scientific and technical knowledge and apply that knowledge to the extent necessary to achieve agency and national goals. Unlike contracts for supplies and services, most R&D contracts are directed toward objectives for which the work or methods cannot be precisely described in advance. It is difficult to judge the probabilities of success or required effort for technical approaches, some of which offer little or no early assurance of full success. (FAR 35.002)

Rather than a "multiyear contract," Thermedics' contract is an R&D contract governed by Part 35 of the FAR. There is no bar in Part 35 of the FAR against R&D contracts extending beyond 5 years. Nor are we aware of any FAR provision limiting an R&D contract such as this to duration of 5 years. As a result, there is no basis to conclude that the agency has impermissibly extended Thermedics' R&D contract. /2/

/2/ The FAR rules governing the use of options in federal contracting bar basic performance periods and option quantities extending beyond 5 years in contracts for supplies or services. FAR Sec. 17.204(e). However, R&D contracts are specifically exempted from these restrictions. FAR Sec. 17.200.

(GAO Decision B-238893)

Incrementally funded projects are those for which budget authority is provided for only part of the estimated cost of a capital acquisition or part of a usable asset...Incremental funding can be justified, however, for high technology capital projects because such projects are often closer in nature to research and development, where useful knowledge can be obtained even if no additional funding is provided. Space exploration equipment would be an example of such a project. (GAO-03-1011)

Capital projects can be grouped into three funding categories: full funding, incremental funding, and high technology... Incrementally funded capital projects are projects for which budget authority is or appears to be provided for only part of the estimated

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cost of a capital acquisition or part of a usable asset. High technology capital projects are incrementally funded projects for which budget authority is or appears to be provided for only part of the estimated cost of information technology acquisitions or projects that are highly dependent on research and development and highly uncertain in outcome. Space exploration equipment would be an example of such a project. Incremental funding can be justified for high technology capital projects because such projects are often closer in nature to research and development and funding provided on an incremental basis can provide useful knowledge even if no additional funding is provided...

Promoting effective management of capital asset acquisitions is important. We recognize that some incremental funding for high technology acquisitions is justified because, while such projects are intended to result in a usable asset, they are closer in nature to research and development activities. However, for other capital projects, as we have previously reported, full funding is an important tool.

*(GAO-01-432R Incremental Funding of Capital Assets)*

**LCS Lead Ships in RDT&E.** As part of its proposed FY2005 and FY2006 budget submissions, the Administration proposed, and Congress approved, funding the two lead Littoral Combat Ships (LCSs) in the Navy's research, development, test and evaluation (RDT&E) account rather than the SCN account, where Navy ships traditionally have been procured. Since the Navy's RDT&E account is outside the procurement title of the defense appropriation act, the ships are not subject to the full funding policy as traditionally applied to DOD procurement programs...

*(CRS Report for Congress: Defense Procurement: Full Funding Policy — Background, issues, and Options for Congress, Updated June 15, 2007)*

## **Appendix B. Funding For Lead DD(X) and Lead LCS**

**Authorization.** The House Armed Services Committee, in its report (H.Rept. 108-491 of May 14, 2004) on the FY2005 defense

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authorization bill (H.R. 4200), stated:

The use of R&D funds for prototypes and truly developmental items is both proper and prudent... While the committee recognizes the increased flexibility of R&D funds in acquiring platforms, there is concern that placing acquisition programs in the R&D budget, particularly at their early, least stable stage, threatens other programs, particularly in science and technology.

**The Senate Armed Services Committee**, in its report (S.Rept. 108-260 of May 11, 2004) on the FY2005 defense authorization bill (S. 2400), stated:

The committee believes that if the flexibility provided by using RDTE,N funds for the lead ship at the lead shipyard is justified, that same flexibility is necessary for the follow ship at the second shipyard as well....

*(CRS Report for Congress: Navy Ship Procurement: Alternative Funding Approaches — Background and Options for Congress, Updated March 25, 2005)*

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**Severable Service**  
(see also  
Nonseverable Service)

- A service that can be separated into components that independently meet a need of the government. The services are continuing and recurring and, by definition, address needs of the time the services are rendered. To the extent a need for a specific portion of continuing or recurring services arises in a subsequent fiscal year, that portion is severable and chargeable to appropriations available in the subsequent year. Funding and period of performance may not extend beyond the appropriation's period of availability unless authorized by statute. Severable service contracts must be funded by an appropriation available for obligation on the date the contractor performs the services.

#### CITATIONS:

Severable Services – Services that are continuing and recurring in nature, and that can be separated into components that independently meet a separate and ongoing need of the government. Common examples are court reporters, court interpreters, local area network and help desk support services, etc. To the extent that a need for a specific portion of a continuing



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service arises in a subsequent fiscal year, that portion is severable and chargeable to appropriations available in the subsequent FY. Generally, severable services must be charged to the fiscal year(s) in which they are rendered.

*(Uscourts.gov's JP3 Glossary of Terms)*

The determining factor for whether services are severable or entire is whether they represent a single undertaking. ///

However, where the services are continuing and recurring in nature, the contract is severable. Service contracts that are "severable" may not cross fiscal year lines unless authorized by statute...Most federal agencies have authority to enter into a 1-year severable service contract, beginning at any time during the fiscal year and extending into the next fiscal year, and to obligate the total amount of the contract to the appropriation current at the time the agency entered into the contract...Otherwise, the services must be charged to the fiscal year(s) in which they are rendered.

*(Red Book, Chapter 5.B.5.)*

For service contracts, whether an expense was properly incurred or properly made during the period of availability depends upon whether the services are severable or nonseverable... Service contracts, where the services are continuing and recurring in nature, such as the vehicle maintenance contract here, are severable and are chargeable to the appropriation current at the time services are rendered. See 60 Comp. Gen. 219, 221 (1981). By definition, severable services address needs of the time the services are rendered.

*(GAO Decision B-259274)*

A task is severable if it can be separated into components that independently meet a separate and ongoing need of the government.<sup>6</sup> Thus to the extent that a need for a specific portion of a continuing service arises in a subsequent fiscal year, that portion is severable and chargeable to appropriations available in the subsequent fiscal year. 60 Comp. Gen. 219, 220-221 (1981). However, where the service provided constitutes a specific, entire job with a defined end-product that cannot feasibly be subdivided for separate performance in each fiscal year, the task should be financed entirely out of the appropriation current at the time of award, notwithstanding that performance may extend into future years. B-240264, February 7, 1994. Thus a nonseverable contract is

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essentially a single undertaking that cannot feasibly be subdivided. B-259274, May 22, 1996. Whether the subdivision is feasible or not is a matter of judgment that includes as a minimum a determination of whether the government has received value from the service rendered. 58 Comp. Gen. 321 (1979). These general rules apply to all fixed period appropriations, whether for one year or three years. 65 Comp. Gen. 170, 171 (1989).  
(GAO Decision B-277165)

Whether an agency should charge the full cost of contract services to the appropriation available on the date a contract for services is made or to the appropriation current at the time services are rendered depends upon whether the services are severable or entire. A task is severable if it can be separated into components that independently meet a separate need of the government. B-235678, above. Thus, to the extent a need for a specific portion of continuing or recurring services arises in a subsequent fiscal year, that portion is severable and chargeable to appropriations available in the subsequent year.  
(GAO Decision B-240264)

4. *Severable Services:*

- a. A service is severable if it can be separated into components that independently meet a need of the government. The services are continuing and recurring in nature.
- b. Severable services thus follow the general service contract Bona Fide Needs Rule, and are the bona fide need of the fiscal year in which performed. Matter of Incremental Funding of Multiyear Contracts, B-241415, 71 Comp. Gen. 428 (1992); EPA Level of Effort Contracts, B-214597, 65 Comp. Gen. 154 (1985). Funding of severable service contracts generally may not cross fiscal years, and agencies must fund severable service contracts with dollars available for obligation on the date the contractor performs the services.

(79th Fiscal Law Course Deskbook, Chapter 3.IV.F.4)

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**Severable Service  
Crossing Fiscal  
Years**

- If express authority exists in law, during the last year in which an appropriation is available for “new” obligations, agencies may enter into a contract for procurement of severable services for a period that begins in one fiscal year and ends in the next fiscal year if (without regard to any option to extend the period of the contract) the contract period does not exceed one year. DoD and USCG may also use this authority for the purpose of leasing real or

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personal property, including the maintenance of such property when contracted for as part of the lease agreement. Funds made available for a fiscal year may be obligated for the total amount of a contract. **Currently, NASA does not have this authority.**

CITATIONS:

(a) Authority.—

(1) The Secretary of Defense, the Secretary of a military department, or the Secretary of Homeland Security with respect to the Coast Guard when it is not operating as a service in the Navy, may enter into a contract for a purpose described in paragraph (2) for a period that begins in one fiscal year and ends in the next fiscal year if (without regard to any option to extend the period of the contract) the contract period does not exceed one year.

(2) The purpose of a contract described in this paragraph is as follows:

(A) The procurement of severable services.

(B) The lease of real or personal property, including the maintenance of such property when contracted for as part of the lease agreement.

(b) Obligation of Funds.— Funds made available for a fiscal year may be obligated for the total amount of a contract entered into under the authority of subsection (a).

*(10 U.S.C. § 2410a)*

(a) Authority

The head of an executive agency may enter into a contract for procurement of severable services for a period that begins in one fiscal year and ends in the next fiscal year if (without regard to any option to extend the period of the contract) the contract period does not exceed one year.

(b) Obligation of funds

Funds made available for a fiscal year may be obligated for the total amount of a contract entered into under the authority of subsection (a) of this section.

*(41 U.S.C. § 3902 [previously in 41 U.S.C. § 253l])*

(a) Applicability of subchapter; delegation of authority

Executive agencies shall make purchases and contracts for property and services in accordance with the provisions of this subchapter and implementing regulations of the Administrator; but this

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subchapter does not apply—

(1) to the Department of Defense, the Coast Guard, and the National Aeronautics and Space Administration;  
(41 U.S.C. § 3101 [previously in 41 U.S.C. § 252])

(b) The head of an executive agency, except NASA, may enter into a contract, exercise an option, or place an order under a contract for severable services for a period that begins in one fiscal year and ends in the next fiscal year if the period of the contract awarded, option exercised, or order placed does not exceed one year (10 U.S.C. 2410a and 41 U.S.C. 2531). *[Note: Content in 41 U.S.C. § 2531 is now covered in 41 U.S.C. § 3902.]* Funds made available for a fiscal year may be obligated for the total amount of an action entered into under this authority.  
(FAR 37.106)

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#### Severable Test

- If a service contract is to be performed partially in one fiscal year and partially in the next and the contract is terminated at the end of the first fiscal year and is not renewed, what do you have? Three examples of applying the severability test are given in GAO's Red Book: "In the case of a window-cleaning contract, you have half of your windows clean, a benefit that is not diminished by the fact that the other half is still dirty. What you paid for the first half has not been wasted. These services are clearly severable. Now consider a contract to conduct a study and prepare a final report, as in 65 Comp. Gen. 741 (1986). If this contract is terminated halfway through, you essentially have nothing. The partial results of an incomplete study, while perhaps beneficial in some ethereal sense, do not do you very much good when what you needed was the complete study and report. Or suppose the contract is to repair a broken frammis. If the repairs are not completed, certainly some work has been done, but you still don't have an operational frammis. The latter two examples are nonseverable." A limitation of funds clause does not affect the applicable bona fide needs rule and the severable test.

#### CITATIONS:

...(subsequent modifications to Fish and Wildlife Service research work orders should be charged to the fiscal year current when the work orders were issued since the purpose of the research is to provide a final research report and the services under the contract are nonseverable).The last opinion is noteworthy because it pointed

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out that a limitation of funds clause does not affect the application of the bona fide needs rule and the severable test. 73 Comp. Gen. at 80... Suppose further that the contract is terminated at the end of the first fiscal year and is not renewed. What do you have? In the case of a window-cleaning contract, you have half of your windows clean, a benefit that is not diminished by the fact that the other half is still dirty. What you paid for the first half has not been wasted. These services are clearly severable. Now consider a contract to conduct a study and prepare a final report, as in 65 Comp. Gen. 741 (1986). If this contract is terminated halfway through, you essentially have nothing. The partial results of an incomplete study, while perhaps beneficial in some ethereal sense, do not do you very much good when what you needed was the complete study and report. Or suppose the contract is to repair a broken frammis.<sup>18</sup> If the repairs are not completed, certainly some work has been done but you still don't have an operational frammis. The latter two examples are nonseverable  
(Red Book, Chapter 5.B.5.)

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**Space Act Agreement** — A binding agreement entered into under the "other transaction" authority in the Space Act between NASA and another party ("Agreement Partner"). Space Act Agreements can be Reimbursable (NASA's costs are reimbursed for its unique goods, services, or facilities), Nonreimbursable (there is no exchange of funds), or Funded (appropriated funds are transferred to a domestic Agreement Partner to accomplish an Agency mission).

As a customer, the obligation is incurred when the agreement is signed and must be funded in accordance with appropriation law. Properly obligated budget authority remains obligated after the appropriation expires for liquidating the ordering agency's obligation as the performing agency completes the work (i.e., it does not have to be deobligated before the appropriation expires, like Economy Act obligations). However, as with other contractual obligations, once the agency liquidates the obligation, any remaining balances are subject to the original purpose and time limitations and are not available for new obligation after the account has expired. "Other transaction" authority is distinguished from contracts in law and by GAO and generally is not subject to federal laws and regulations applicable to procurement contracts, but they are subject to Appropriation Law requirements.

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## CITATIONS:

Space Act Agreements (herein "Agreement(s)") entered into under the "other transaction" authority in the Space Act establish a set of legally enforceable promises between NASA and the other party to the Agreement (herein "Agreement Partner"). Such Agreements constitute Agency commitments of resources (including personnel, funding, services, equipment, expertise, information, or facilities) to accomplish stated objectives of a joint undertaking with an Agreement Partner... ///

The Space Act provides authority for Reimbursable, Nonreimbursable, and Funded Agreements. In this NPD, each type of Agreement is defined and differentiated by underlying principles, as follows, to ensure that each type of Agreement is effectively utilized and strategically managed:

a. Reimbursable Agreements are Agreements wherein NASA's costs associated with the undertaking are reimbursed by the Agreement Partner (in full or in part). NASA undertakes Reimbursable Agreements when it has unique goods, services, and facilities not being fully utilized to accomplish mission needs, which it can make available to others on a noninterference basis, consistent with the Agency's missions...

b. Nonreimbursable Agreements involve NASA and one or more Agreement Partners in a mutually beneficial activity that furthers the Agency's missions, wherein each party bears the cost of its participation, and there is no exchange of funds between the parties...

c. Funded Agreements are Agreements under which appropriated funds are transferred to a domestic Agreement Partner to accomplish an Agency mission...

*(NASA Policy Document ( NPD) 1050.1, Section 1.)*

For our purposes here, while the Economy Act, like other interagency transaction authorities, requires the ordering agency to obligate its appropriation when it enters into an agreement with another federal agency, if the appropriation charged is a fiscal-year appropriation, the Economy Act requires the ordering agency to deobligate the appropriation at the end of the fiscal year to the extent that the performing agency has not performed. 31 U.S.C. § 1535(d). See, e.g., 39 Comp. Gen. 317 (1959); 34 Comp. Gen. 418, 421-22 (1955). That requirement is specific to Economy Act transactions and does not apply to transactions governed by

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statutory authority other than the Economy Act.  
(GAO Decision B-302760)

without regard to subsections (a) and (b) of section 3324 of title 31, to enter into and perform such contracts, leases, cooperative agreements, or other transactions as may be necessary in the conduct of its work and on such terms as it may deem appropriate, with any agency or instrumentality of the United States, or with any State, territory, or possession, or with any political subdivision thereof, or with any person, firm, association, corporation, or educational institution. To the maximum extent practicable and consistent with the accomplishment of the purpose of this chapter, such contracts, leases, agreements, and other transactions shall be allocated by the Administrator in a manner which will enable small-business concerns to participate equitably and proportionately in the conduct of the work of the Administration.  
(51 U.S.C. § 20113(e) [formerly in 42 U.S.C. § 2473(c)(5)])

(a) Except as provided in this section, a payment under a contract to provide a service or deliver an article for the United States Government may not be more than the value of the service already provided or the article already delivered.

(b) An advance of public money may be made only if it is authorized by...  
(31 U.S.C. §3324)

An other transaction (OT) is a special vehicle used by federal agencies for obtaining or advancing research and development (R&D) or prototypes. An OT is not a contract, grant, or cooperative agreement, and there is no statutory or regulatory definition of “other transaction.” Only those agencies that have been provided OT authority may engage in other transactions. /// OT authority originated with the National Aeronautics and Space Administration (NASA) when the National Aeronautics and Space Act of 1958 was enacted... ///

Generally, the reason for creating OT authority is that the government needs to obtain leading-edge R&D (and prototypes) from commercial sources, but some companies (and other entities) are unwilling or unable to comply with the government’s procurement regulations.

(CRS Report for Congress: Other Transaction (OT) Authority)



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Under the Competition in Contracting Act of 1984 and GAO's Bid Protest Regulations, GAO will not review the issuance of Space Act agreements pursuant to agency's "other transactions" authority, because the issuance of the Space Act agreements pursuant to that authority was not tantamount to the award of contracts for the procurement of goods and services and was, therefore, outside GAO's bid protest jurisdiction...

"Space Act" agreements are issued by NASA under its "other transactions" authority pursuant to the National Aeronautics and Space Act of 1958 (the "Space Act"). 42 U.S.C. § 2473(c)(5) (2000). *[Note: Content in 42 U.S.C. § 2473(c)(5) is now covered in 51 U.S.C. § 20113(e).]* A "Funded Space Act Agreement" is "an agreement under which appropriated funds will be transferred to a domestic agreement partner to accomplish an Agency mission, but whose objective cannot be accomplished by the use of a contract, grant, or Chiles Act cooperative agreement." NASA Policy Directive, NPD 1050.1G, Nov. 13, 1998, at 1-2...

GAO's reports to Congress have also reported that "other transactions" are "other than contracts, grants, or cooperative agreements that generally are not subject to federal laws and regulations applicable to procurement contracts."

*(GAO Decision B-298804)*

In April 2000, we reported on the Department of Defense's (DOD) use of Section 845 agreements, also referred to as "other transactions" for prototype projects. These are transactions other than contracts, grants, or cooperative agreements that generally are not subject to federal laws and regulations applicable to procurement contracts.

*(GAO-03-150)*

A binding agreement entered into under the "other transaction" authority in the Space Act between NASA and another party ("Agreement Partner"). Space Act Agreements can be Reimbursable (NASA's costs are reimbursed for its unique goods, services, or facilities), Nonreimbursable (there is no exchange of funds), or Funded (appropriated funds are transferred to a domestic Agreement Partner to accomplish an Agency mission). Properly obligated budget authority remains obligated after the appropriation expires for liquidating the ordering agency's obligation as the performing agency completes the work (i.e., it



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does not have to be deobligated before the appropriation expires, like Economy Act obligations). However, as with other contractual obligations, once the agency liquidates the obligation, any remaining balances are subject to the original purpose and time limitations and are not available for new obligation after the account has expired. "Other transaction" authority is distinguished from contracts in law and by GAO and generally is not subject to federal laws and regulations applicable to procurement contracts. *(NPR 9470.1)*

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- Special Termination** — An agreement to pay “special termination” costs under an incrementally funded contract creates a firm obligation, not a contingent liability, to pay the contractor because the contracting agency remains liable for the costs even if it decides not to fund the contract further.

Record the obligation when the agreement is signed. This obligation remains until the contract is fully funded.

**CITATIONS:**

An agreement to pay “special termination” costs under an incrementally funded contract creates a firm obligation, not a contingent liability, to pay the contractor because the contracting agency remains liable for the costs even if it decides not to fund the contract further.  
*(Red Book, Chapter 6.C.2.b.(3))*

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- Technology Development/  
High Technology** — (See R&D/Technology Development Contracts.)
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